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# Rediscovering Usury: An Argument for Legal Controls on Credit Card Interest Rates.

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**REDISCOVERING USURY: AN ARGUMENT  
FOR LEGAL CONTROLS ON CREDIT CARD  
INTEREST RATES**

BY VINCENT D. ROUGEAU\*

*Men are qualified for civil liberty, in exact proportion to their disposition to put moral chains upon their own appetites; in proportion as their love to justice is above their rapacity . . . . Society cannot exist unless a controlling power upon will and appetite be placed somewhere, and the less of it there is within, the more there must be without. It is ordained in the eternal constitution of things, that men of intemperate minds cannot be free. Their passions forge their fetters.<sup>1</sup>*

INTRODUCTION

Americans are known around the world for their love of shopping and the abundance of material comforts in their lives. Washing machines, color televisions, video cassette recorders, microwave ovens, telephones, and automobiles are not considered luxuries for most Americans, regardless of income.<sup>2</sup> American economic policy is heavily oriented toward consumption, and it is consumer spending, more often than not, that carries the

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1. EDMUND BURKE, LETTER TO A MEMBER OF THE NATIONAL ASSEMBLY (1791), reprinted in VII THE WRITINGS AND SPEECHES OF EDMUND BURKE: THE FRENCH REVOLUTION 1790-1794, at 332 (L.G. Mitchell ed., 1989).

2. In 1987, at least two-thirds of American households had washing machines, color televisions, and microwaves. JULIET B. SCHOR, THE OVERWORKED AMERICAN: THE UNEXPECTED DECLINE OF LEISURE 111-12 (1991).

economy in and out of economic recessions.<sup>3</sup> Over the last twenty years, various sectors of the American economy have been deregulated under the assumption that free markets, unfettered by burdensome government regulation, would produce increased competition and greater economic efficiency. A more efficient economy would produce more and better goods at lower prices, which would increase consumption and make the nation wealthier and thus "better off." During the same period, the economic theories that spawned deregulation increasingly found their way into aspects of American life beyond the traditional economic sphere. In a culturally contentious society faced with the demands of an increasingly global economy, the "rational" and purportedly "value-neutral" arguments of the market found widespread legitimacy as the language of fairness, reason, and material progress. At the same time, however, the legal and cultural constraints on free-market ideas that traditionally had been used to temper the effects of economic activity in order to fit it within a broader social context were increasingly marginalized.

This article explores the specific question of setting a legal maximum for credit card interest rates. There has been extensive discussion in the popular press of the explosion of credit card use and the extraordinarily high interest rates people are willing to pay, through various fees and interest charges, to use them. Classic free-market economic arguments have been used to prevent the imposition of a federal cap on credit card interest rates, but there is strong evidence that economic models inadequately explain the credit card market and that a lack of interest rate controls has produced a dramatic transfer of wealth from consumers to the major credit card issuers, most of which are large national banks.<sup>4</sup> I argue that this absence of regulation,

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3. Close to two-thirds of the nation's gross domestic product ("GDP") is made up of personal consumption expenditures. U.S. BUREAU OF THE CENSUS, STATISTICAL ABSTRACT OF THE UNITED STATES: 1994, at 446 (114th Ed. 1994) [hereinafter STATISTICAL ABSTRACT]. The total GDP in 1993 (in constant 1987 dollars) was \$5,136 billion, \$3,453.2 billion of which was devoted to personal consumption. *Id.*

4. The ten largest credit card issuers in the United States are, in rank order: (1) Citicorp; (2) Sears Discover; (3) Chase Manhattan; (4) MBNA America; (5) First Chicago; (6) Bank of America; (7) AT&T Universal; (8) Chemical Bank; (9) Household Bank; and (10) Bank of New York. GENERAL ACCT. OFFICE, U.S. CREDIT CARD INDUSTRY—COMPETITIVE DEVELOPMENTS NEED TO BE CLOSELY MONITORED, GAO/GGD 94-23, 20-21 (Apr. 28, 1994) [hereinafter GAO REPORT]. At a symposium on bankruptcy law and financial institutions, which was part of the Fifth Annual Lawyers Convention sponsored by the Federalist Society at Cornell Law School in

which relies primarily on traditional liberal economic arguments for support, either (1) ignores the irrational nature of a consumer culture and promotes an extremely limited view of what is good social and economic policy, or (2) understands the irrational nature of consumers all too well and is designed to confer special benefits on the lenders of money. The result is a legal policy that promotes consumption and acquisitiveness and encourages behavior, such as greed, that the culture has traditionally labeled undesirable. After I observe the "real world" activity of a large number of credit card holders and examine effects this prevailing legal regime has had on consumers, I make two major arguments. First, allowing the market alone to set interest rates on credit cards is a one-sided legal policy that promotes consumption and debt among consumers, while producing unusually high profits for credit card issuers. Moreover, adherence to this one-sided policy has allowed the law to become a tool of the special interests that benefit from the promotion of high consumer debt and consumption. Second, the establishment of realistic interest rate controls in the credit card market would be preferable to the present system for two important reasons: (1) as a legal policy, interest rate controls more fairly balance the interests of consumers and credit card issuers than the current laissez-faire policy; and (2) the market is not an entity that exists separately from the larger cultural values and traditions of our society. Usury laws have been used throughout history to exercise social control over economic relationships that, unchecked, tend to degenerate into exploitation and other socially counterproductive behavior.

Part I of this article examines the current state of the credit card industry and reviews the major legislative and judicial developments over the last twenty years that effectively have deregulated credit card interest rates. Part II explores the economic arguments against interest rate regulation and examines important weaknesses in these arguments as they apply to the credit card market. Part III presents challenges to some of the accepted economic arguments supporting deregulation and raises some additional arguments concerning the

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1992, Professor Elizabeth Warren of the University of Pennsylvania noted that huge profits on credit cards were saving some of the nation's largest banks from financial disaster. Elizabeth Warren, *Why Have a Federal Bankruptcy System*, 77 CORNELL L. REV. 1093 (1992). Losses from bad loans to developing countries and poor real-estate lending were being covered by credit card profits. *Id.*

negative effects of a lack of interest rate controls on credit cards. Finally, Part IV offers some general observations about reforming the credit card market and argues that reasonable interest rate controls, although they may tend to restrict the amount of credit available, are essential because they help to keep market interactions in line with important values of the larger culture.

## I. THE GROWTH OF THE CREDIT CARD INDUSTRY AND INTEREST RATE DEREGULATION

### A. *The Growth of the Credit Card Industry*

Credit cards have revolutionized the way Americans live and how they spend their money.<sup>5</sup> In the United States, large retailers were the first to issue the "charga-plates" that eventually became the credit cards of today.<sup>6</sup> Charga-plates, which first appeared in the late 1920s, resembled military dogtags and were issued to a store's better customers to allow them to post purchases to a store account.<sup>7</sup> Today, retailers still form an important part of the credit card market, but it is the third-party universal card that is now preeminent. First created by Diner's Club in 1949, the universal card was accepted in a variety of places and used a third party to extend credit to the customer and

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5. For the purposes of this article, I define credit cards as those cards that allow an account holder to make retail purchases by presenting the card to a merchant who will be paid by the issuer of the card. The account holder will then receive a statement from the card issuer detailing the purchases that were made during the statement period. The statement can be paid upon receipt (in many cases there is a "grace" period of 25 to 30 days) and no interest charges will accrue or a small payment may be made (typically 2.5% of the outstanding balance) to keep the account current. The remaining amount is deducted from the cardholder's line of credit and the unpaid amount may be paid at the cardholder's convenience. Interest charges accrue on this unpaid balance until it has been repaid. Banks are the major issuers of credit cards today, but department stores and other retailers also make up a large part of the market. There is an important distinction between *credit* cards and *debit* cards. Debit cards are linked to an account at a financial institution and the money necessary to cover a purchase is subtracted from the account as the purchases are made. Thus a debit card is not a means for extending credit. In most other respects, however, they are indistinguishable from credit cards.

6. Oil companies and, later, airlines began issuing plates during the same period for fuel and travel. LEWIS MANDELL, *THE CREDIT CARD INDUSTRY: A HISTORY* xii (1990). Mandell makes extensive use of the *Nilson Report*, which is a monthly publication that chronicles developments in the credit card industry.

7. *Id.* at xiii.

to pay the merchant.<sup>8</sup> American Express soon followed Diner's Club into the market with a competing universal card, and it remains a dominant force in the credit card market today. The vast majority of universal credit cards, however, are now issued by banks and carry the logo of "VISA" or "MasterCard".<sup>9</sup>

Once a consumer makes an initial application for a credit card and the application is accepted, she need never again suffer the indignity of having her credit history reviewed or her spending patterns scrutinized by the card issuer. In fact, the approval process for many credit cards is often almost automatic, with only those with the worst credit ratings being turned away.<sup>10</sup> Consequently, while early credit cards were essentially a privilege for the wealthy or businessmen on expense accounts, credit card use among Americans today is widespread in all socioeconomic groups.<sup>11</sup> Increasing the amount one is eligible to borrow (that is, one's "credit line" or "credit limit") often requires nothing more than a telephone call and, in many cases, the card issuer will increase the credit limit without solicitation. Thus, purchases that thirty years ago would have required for most

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8. *Id.*

9. *Id.* at 26, 51. Of the \$539 billion in credit card spending in the United States in 1992, approximately \$390 billion was spent on bank, travel, and entertainment cards. STATISTICAL ABSTRACT, *supra* note 3, at 522. The overwhelming majority of the remaining spending was on cards issued by department stores. *Id.*

10. Department stores are notorious for extending "instant credit" and often offer discounts on purchases at the point of sale if the customer agrees to accept a charge account with the retailer. In many instances, it is not even necessary to have a job or a credit history in order to receive a credit card. Indeed, a substantial portion of credit card marketing is directed at those with poor credit ratings, or those with no credit rating at all. Most American cities are filled with advertising on public transportation directed at these consumers ("Bad Credit? No Credit? We have a Visa card just for you!"). Some of these cards must be secured with a cash payment, but many do not have such a requirement. High interest rates are generally used to compensate lenders for any increased risk. College and graduate students, who more often than not have no credit history and no regular source of income, are heavily solicited. For a more complete discussion of credit card marketing among high school and university students, see *infra* notes 118-125 and accompanying text.

11. In 1989, 68% of all U.S. households had some type of credit card (e.g., bank, store, gasoline). Glenn B. Canner & Charles A. Luckett, *Developments in the Pricing of Credit Card Services*, 78 FED. RESERVE BULL. 652, 656 (Sept. 1992) [hereinafter *Credit Card Study*]. The only income group in which less than 50% of the families had credit cards (30%) was the one in which incomes were below \$10,000 per year. *Id.* at 656. Notably, that income group is well below the official poverty line, which in 1989 was \$12,674 for a family of four. STATISTICAL ABSTRACT, *supra* note 3, at 475. In families earning more than \$50,000 per year, 95% had credit cards, and the mean number of accounts for all families was 5.6. *Credit Card Study*, *supra*, at 656.

Americans months of saving or an uncomfortable meeting with a loan officer at a bank or thrift institution are now made instantly, simply by presenting a plastic card.<sup>12</sup>

Of the top fifty credit card issuers in the United States, thirty-seven are banking or thrift institutions.<sup>13</sup> The remaining thirteen companies are large diversified corporations such as Sears, AT&T, and American Express.<sup>14</sup> The top fifty issuers of credit cards control close to 75% of the credit card market, but the real market power rests with the top twenty-five who control 65% of the credit card marketplace.<sup>15</sup> After struggling during the 1960s and 1970s, consumers' credit card use and banks' profits from credit card operations exploded during the 1980s.<sup>16</sup> In 1989, people in more than 54% of American households had credit cards; at the same time, credit cards have become the most profitable aspect of the banking business.<sup>17</sup>

Credit cards have moved the United States inexorably toward the "cashless society" envisioned as the wave of the future since the nineteenth century.<sup>18</sup> They have become such an important

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12. Apart from the economic changes credit card use has promoted, it is important to note the social and cultural changes that have occurred at the same time. When credit card companies were soliciting widely in the early 1970s, they found it very difficult to earn profits because most of their customers, generally 70% to 80%, paid their balances before they accrued interest. MANDELL, *supra* note 6, at 71. This situation has practically reversed itself today. See *infra* note 22 and accompanying text.

13. Mickey Meese & L. Michael Cacace, *Nonbanks Gain Ground in the Credit Card Race Series*, AM. BANKER, Sept. 20, 1993 at 1.

14. *Id.* at 1-3.

15. *Id.* at 2. The top ten issuers of credit cards control 57% of the market. GAO REPORT, *supra* note 4, at 20-21.

16. GAO REPORT, *supra* note 4, at 12.

17. The credit card business was tremendously profitable throughout most of the 1980s, with returns on assets that far exceeded those for other areas of the banking business. See generally Lawrence M. Ausubel, *The Failure of Competition in the Credit Card Market*, AM. ECON. REV., Mar. 1991, at 50, 56-64. This high level of profitability has continued in the 1990s. See *Banking Industry Reaps Credit Card Profits*, CARD FAX, Apr. 4, 1994; *Competition: The Credit Card Industry Rides a Wave of Profitability*, 24 CREDIT CARD NEWS 6, April 1, 1994, available in WESTLAW, CRC DNS database.

18. In the 1880s, Edward Bellamy predicted that the demonetization of gold and its abandonment as a medium of exchange would bring about a new, less materialistic age. He used the year 2000 as his benchmark for the new era. EDWARD BELLAMY, *LOOKING BACKWARD: 2000-1887* (Signet Classic, 1960) (1887). By the 1960s and 1970s economic scholars were convinced that, at least in wealthy industrialized states of the world, the cashless society was indeed becoming a reality. See generally ROBERT A. HENDRICKSON, *THE CASHLESS SOCIETY* (1972). Hendrickson saw the disappearance of a cash economy as a positive development, decreasing opportunities

part of everyday life in this country that it can be quite difficult to conduct one's affairs without them.<sup>19</sup> But easy, unsecured credit has never come cheap. The price the typical American credit card holder pays for all of this convenience is extremely high. Most credit cards carry an annual fee, ranging from \$15 to \$40 (and as high as \$300 for certain prestige cards).<sup>20</sup> Americans carry an average outstanding balance of \$1,700 on a typical credit card at an average interest rate of 17.66%.<sup>21</sup> It is, of course,

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for fraud and furthering the creation of an efficient international economy. *Id.* at 223-45. For most transactions, he suggested a single national credit card for each American under the supervision of the Federal Reserve or a central credit administration. *Id.* at 234-40. Special tokens or coins would be issued for small transactions and for tolls and vending machines. *Id.* at 235. Of course, in 1994, we already have systems in place that will eliminate the need for cash in those areas as well. Plans are well underway to introduce "electronic purses" to consumers throughout the United States. These wallet-sized cards are embedded with rechargeable microchips that store sums of money and are designed to compete with cash for transactions under twenty dollars. See, Saul Hansell, *An End to the "Nightmare" of Cash*, N.Y. TIMES, Sept. 6, 1994, at D1.

19. Credit cards are required as security for renting so many items, such as cars, hotel rooms, and movies, that it would be impossible to list them all. One could of course use cash as security, but most people find this risky and inconvenient for obvious reasons. After a purchase has been made, credit cards also allow for easier returns and refunds. In printed testimony submitted to the House Subcommittee on Consumer Credit and Insurance in March 1994, Visa, U.S.A., stated that "[i]t is impossible in today's world to order merchandise by mail, rent a car, buy an airline ticket, or do many routine things without a plastic payment card of some kind." *Bankcards and the College Market: Hearings Testimony Before the Subcomm. on Consumer Credit and Insurance of the House Comm. on Banking, Finance, and Urban Affairs*, 103rd Cong., 2d Sess. (Mar. 10, 1994). Even grocery stores now accept credit cards, which would have been unheard of just a few years ago. Gary Levin, *Credit Cards Bagging More Grocery Sales*, ADVERTISING AGE, Jan. 4, 1993, at 12. The idea of paying for the necessities of life with a credit card (or on credit) conjures up images of a descent into inescapable debt, and consumer advocates have been quite concerned about this new development in credit card use. Andrew Leckey, *Think Twice Before Charging Grocery Items*, ST. LOUIS POST DISPATCH, Mar. 11, 1994, at 13D.

20. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, FEDERAL RESERVE STATISTICAL RELEASE, REPORT ON THE TERMS OF CREDIT CARD PLANS, Sept. 12, 1994. Information collected from a large cross section of the bank issuers of credit cards every six months by the Federal Reserve indicates that as of September 1994, only 45 of 149 issuers surveyed, or approximately 30%, offer cards with no annual fee. *Id.* While preparing this article, I received two solicitations for the American Express Platinum Card. The card provides numerous benefits and services and carries a yearly fee of \$300.

21. Robert D. Hershey, Jr., *Americans Buying More On Credit*, N.Y. TIMES, July 30, 1994, at 33. The 17.66% figure is for bank cards, which comprise most of the credit card market. *Id.* There were many new cards with lower rates introduced during the past few years and many of those rates are tied to the prime rate. GAO REPORT, *supra* note 4, at 14. For example, in March, 1993, 63 of 152 card issuers



possible to avoid interest rate charges on credit cards by paying off the balance every month, but the vast majority of credit card holders do not, or can not, do this.<sup>22</sup> In 1992, the amount of credit card debt outstanding was \$273 billion, which compares to credit card spending of \$539 billion in the same year; credit card debt is expected to rise to \$436.8 billion and credit card spending to rise to \$1,004 billion by the year 2000.<sup>23</sup> Despite a growing number of credit card issuers entering the business and an almost constant introduction of new types of cards, the credit card business remains extremely lucrative.<sup>24</sup>

When a credit card is used to make a purchase, the cardholder has received an unsecured loan from the card issuer. Interest could accrue immediately, but under most credit card agreements there is a "grace period" of 25-30 days during which no interest is owed.<sup>25</sup> Borrowing money without security is almost always more expensive than when a loan is secured by some form of collateral, because the lender is relying only on the borrower's legally binding promise to pay as a guarantee of repayment. Higher interest rates compensate the lender for the higher risk of borrower default. From the colonial era through the 1970s, most states controlled interest rates on unsecured consumer loans, but by the late 1970s, due to high inflation and extremely high interest rates for money in commercial markets,

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reporting to the Federal Reserve, or approximately 40%, charged a variable rate. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, FEDERAL RESERVE STATISTICAL RELEASE, REPORT ON THE TERMS OF CREDIT CARD, Mar. 15, 1993. By September, 1994, the numbers had changed to 90 of 149 reporting, or approximately 60%. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, FEDERAL RESERVE STATISTICAL RELEASE, REPORT ON THE TERMS OF CREDIT CARD, Sept. 12, 1994.

22. Close to 70% of all credit card holders maintain outstanding balances. Hershey, *supra* note 21, at 33. A general rule of thumb in the credit card industry is that 90% of an issuer's outstanding balances accrue interest. Ausubel, *supra* note 17, at 58 n.20. Of course, these payments could range from just a few dollars a year to several hundred or more. Nevertheless, the Federal Reserve has found that consumers tend to overstate the number of times they pay their bills in full. *Credit Card Study*, *supra* note 11, at 663.

23. STATISTICAL ABSTRACT, *supra* note 3, at 522.

24. In 1993, the banking industry's profit was a record \$43.4 billion. *Competition: The Credit Card Industry Rides a Wave of Profitability*, *supra* note 17. Visa and MasterCard card profits totaled \$4.4 billion after taxes in 1993, up from \$3.4 billion in 1992. *Id.* Credit card returns on assets were 2.3% in 1993 and 2.0% in 1992, which is about twice as high a rate of return on assets as that of the banking industry as a whole. *Id.*

25. Ann Perry, *Check the Fine Print on Credit-Card Offers*, SAN DIEGO UNION TRIBUNE, July 16, 1995, at I1.

the ceilings set by many states were too low to make consumer lending profitable.<sup>26</sup> During this same period, banks were becoming increasingly active in the credit card market. Many banks saw tremendous business potential in this form of consumer credit, but they were prevented from charging market interest rates due to state usury laws.<sup>27</sup>

### *B. Deregulation of Interest Rates*

In 1978, the Supreme Court rendered a decision that would prove to have tremendous ramifications for the growth of the credit card business in the United States. In *Marquette National Bank of Minneapolis v. First of Omaha Service Corp.* ("Marquette"), the Court ruled that section 85 of the National Bank Act allowed a national bank to charge its credit card customers the highest interest rate permitted in the bank's home state, regardless of the interest rate limitations prevailing in the customer's state of residence.<sup>28</sup> The Court was primarily concerned with interpreting the language and history of section 85, but the solicitor general of Minnesota, attempting to prevent First Omaha from soliciting credit card customers in Minnesota at higher Nebraska interest rates, also contended that allowing the exportation of Nebraska's interest rates would make it very difficult for states to enact effective usury laws.<sup>29</sup> Although the

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26. MANDELL, *supra* note 6, at 12.

27. MANDELL, *supra* note 6, at 70-72, 78-79.

28. 439 U.S. 299, 307-19 (1978). Section 85 of the National Bank Act states in relevant part:

Any association may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidence of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located, or at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and no more, except that where by the laws of any State a different rate is limited for banks organized under state laws, the rate so limited shall be allowed for associations organized or existing in any such State under this chapter [title 62 of the Revised Statutes]. When no rate is fixed by the laws of the State, or Territory, or District, the bank may take, receive, reserve, or charge a rate not exceeding 7 per centum, or 1 per centum in excess of the discount rate on ninety day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater . . . .

12 U.S.C. § 85 (1994).

29. 439 U.S. at 318.

Court agreed that such might indeed be the case, it saw the usury issue as a legislative problem to be handled by Congress.<sup>30</sup> Thus, after *Marquette*, a state with more restrictive usury laws could no longer protect its citizens from an interest rate charged by an out-of-state bank that was higher than the state's legal maximum, so long as the rate was allowable in the bank's home state.

In the wake of *Marquette*, states with no usury laws, or those with the highest legal maximums, became ideal locations for national banks to set up credit card operations. Indeed, shortly after the *Marquette* decision, several states repealed their usury restrictions or raised the maximum interest rate that could be charged on a consumer loan.<sup>31</sup> Major issuers, such as Citibank and Maryland Bank, N.A., moved their credit card operations to escape the usury laws in their home states, often using the threat of lost jobs to pressure their home state legislators into liberalizing the usury statutes.<sup>32</sup> The credit cards were marketed nationally from the new locations, and the usury limits of the customers' states of residence became irrelevant. The *Marquette* decision thus had the net effect of deregulating interest rates in the credit card market.

In the early 1980s, high credit card interest rates were in step with the interest rates that were then prevalent in the economy for all kinds of loans. But this period was anomalous. By the mid-1980s, interest rates began to drop. Credit card interest rates, however, remained steady. From 1972 to 1992, the average interest rate on credit cards in the United States

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30. 439 U.S. at 319.

31. *Marquette* essentially ushered in an era of interest rate competition among the states, and individual states could no longer effectively govern the credit card transactions of their residents. See Donald C. Langevoort, *Statutory Obsolescence and the Judicial Process: The Revisionist Role of the Courts in Federal Banking Regulation*, 85 MICH. L. REV. 672, 685-86 (1987).

32. In the years following *Marquette*, many major banks used the threat of lost jobs to pressure states into relaxing or ending interest rate regulation. These were not idle threats. When the Maryland legislature capped interest rates at a level that the Maryland National Bank, one of the largest card issuers in the country, thought was too low for its credit card operations, those operations, and the credit card operations of several other major Maryland banks, moved to Delaware. Alison Muscatine, *Fourth Maryland Bank Plans Credit Card Operations Move*, WASH. POST, Mar. 26, 1982, at B1. Delaware set no limit on interest rates and permitted banks to charge additional fees on credit cards that were forbidden in Maryland and many other states, which attracted credit card operations from around the country. 2 Mich. Banks Hint Delaware Move, While Maryland National Does It, AMERICAN BANKER, Mar. 4, 1982, at 2.

remained between 17% and 19%.<sup>33</sup> During the same time period, the average rates on most other types of loans, including consumer loans, fluctuated over a range of at least eight percentage points and dropped steadily from a peak in 1981.<sup>34</sup> By 1992, the prime rate had dropped to six percent, where it remained through 1993, making the average credit card interest rate eleven to thirteen percentage points higher than the prime lending rate.<sup>35</sup>

### 1. After Deregulation: Legislative Responses to High Credit Card Interest Rates

High rates for credit card borrowing have not gone unnoticed. During 1987, when the prime rate dropped below nine percent, Congress considered a federal cap for credit card interest rates.<sup>36</sup> Although the legislative activity did not produce an interest rate ceiling, it did result in legislation that mandated better disclosure by credit card issuers of important information on the terms of credit card plans.<sup>37</sup> More recently, a brief but rather intense battle was fought on Capitol Hill over the issue of credit card interest rates. In November of 1991, President Bush, facing an election and an economy in decline, mentioned off-handedly that

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33. *Credit Card Study*, *supra* note 11, at 652.

34. *Id.* It is interesting to note that even when these rates were at their highest, they were still lower than the average rate for credit cards. *Id.*

35. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, FEDERAL RESERVE STATISTICAL RELEASE, MONTHLY INTEREST RATES: JANUARY 1, 1970 TO DECEMBER 31, 1993. Average credit card rates declined to 16.8% in 1993. GAO REPORT, *supra* note 4, at 13. The difference between the average credit card rate and the cost of funds was nevertheless 11.50%, the highest level since 1976. *Id.* at 14.

36. In 1988, Congress passed the Fair Credit and Charge Card Disclosure Act of 1988, which preempted state statutes and mandated disclosure of various information on credit card interest rates, fees, and conditions. Fair Credit and Charge Card Disclosure Act of 1988, 15 U.S.C. § 1637 (1994). In the House version, the bill also contained an amendment that would have capped credit card interest rates by floating those rates at 8% above the yield of one-year Treasury securities. Although the disclosure bill passed almost unanimously in the House (there was one dissenting vote), the amendment was defeated 356 to 56. Nancy L. Ross, *House Passes Credit Card Disclosure Bill*, WASH. POST, Oct. 29, 1987, at E2.

37. In passing this legislation, Congress chose a "disclosure approach" to deal with the problem of high credit card interest rates. Accepting the assumptions of free-market economic theory, Congress hoped to promote a more competitive credit card market by increasing the amount of information on revolving credit available to consumers. It was hoped that consumers would comparison shop and that this process would force card issuers to offer better deals. For a more complete review of the congressional discussions surrounding the legislation, see S. REP. NO. 259, 100th Cong., 2d Sess. (1988), *reprinted in* 1988 U.S.C.C.A.N. 3936-3962.

perhaps credit card interest rates were too high and that this situation was not helping consumer spending.<sup>38</sup> Congress immediately seized the issue. Within days, the Senate had voted in favor of a federally mandated cap on credit card interest rates, and it was assumed that the House would follow shortly thereafter.<sup>39</sup>

On November 15, the Dow Jones Industrial Average plummeted 120 points, with some bank stocks losing as much as ten percent of their value. To protest the pending congressional action, banks threatened to cancel the credit cards of as many as half of the people who held them at that time.<sup>40</sup> Soon President Bush retreated from his earlier statement, suggesting that rate caps were unwise. The Democratic leadership of the House announced that they agreed with the President, and the legislation died. Bank stocks rallied and continued to climb well into 1992.<sup>41</sup>

## 2. Accepting Deregulation: Justifications for the High Cost of Deregulated Credit

These historical episodes suggest that even the nation's leaders have been uncomfortable with the consistently high credit card interest rates over the last decade and a half, particularly in the low interest rate economy of the late 1980s and early 1990s. They have been unable, however, to resist the tremendous lobbying power of the banking industry and the appeal of economic arguments against interest rate regulation. During the 1987 and 1991 debates over federal interest rate caps, as well as in the years since, credit card issuers have offered two primary reasons to explain the high cost of their credit.

The first centers on the issue of cost. Card issuers contend that providing revolving credit through the vehicle of credit cards

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38. John R. Cranford, *Cap for Credit Card Rates Catches Fire*, 49 CONG. Q. 3364 (1991). The President was relying on consumer spending to pull the nation out of a recession, despite the fact that, because of the recession, many consumers had lost their jobs or were underemployed. *Id.*

39. *Id.*

40. John R. Cranford, *Credit Card Rate Cap: Flash in Pan*, 49 CONG. Q. 3442 (1991); Albert B. Crenshaw & Kara Swisher, *Bank Industry Says Rate Cap Would Cost Many Their Credit Cards*, WASH. POST, Nov. 15, 1991, at D1.

41. Crenshaw & Swisher, *supra* note 40, at D1; See James J. Cramer, *Card Sharks*, THE NEW REPUBLIC, Oct. 26, 1992, at 19.

is expensive. When banks initially began issuing credit cards in large numbers there were high start-up costs, relatively low receivables, and state usury ceilings that prevented an upward adjustment of interest rates.<sup>42</sup> Once usury restrictions were removed or minimized, banks still had to contend with the higher operating costs and higher default risks per dollar of receivables in the credit card business than in other types of bank lending.<sup>43</sup> Because most credit cards are unsecured, the risks of default are generally higher than is typical for other bank loans. The charge-off rate for credit card operations (that is, losses sustained due to uncollectible accounts) is substantially higher than that for other types of bank lending, and the costs associated with processing a large number of relatively small transactions are considerable.<sup>44</sup> The high level of additional expenses means that the cost of funds comprises a smaller portion of the cost of credit card operations. For credit card lending, then, there must be larger differences between interest rate indicators in the market (such as the prime rate) and credit card interest rates.<sup>45</sup> I will refer to this as the "cost argument."

The second argument is inspired by liberal economic theory and is rooted in ideas about individual choice and the operation of the free market. If they so choose, card issuers note, consumers always have the option of securing credit through less expensive vehicles. In the last few years, partly in response to the attempt to control card rates in 1991, more card issuers have offered adjustable-rate cards and lower-rate cards tied to the prime rate or other major interest rate indices.<sup>46</sup> Card issuers argue that any cap on interest rates would simply limit the credit options available to consumers as a group. As is the case with the lower-interest cards being marketed today, lower rates would be given only to customers who were perceived by the issuers as lower risk. Card issuers would offer fewer products and consumers applying for cards would have to be more creditworthy. Many

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42. Through most of the 1970s and early 1980s, credit card operations were the least profitable of all bank operations. MANDELL, *supra* note 6, at 78.

43. GAO Report, *supra* note 4, at 24; Arthur P. Hall & J. Marc Wheat, *Do Credit Cards Need Interest Rate Caps?*, CONSUMERS' RES., Feb. 1992, at 30-31.

44. *Credit Card Study*, *supra* note 11, at 658.

45. *Id.* at 660. The cost of funds generally comprises 25% to 50% of the cost of credit card operations. *Id.* See also Hillary Rule, *Credit Card Interest Rates and Their Immunity to Market Fluctuations*, 7 ANN. REV. BANKING L. 463, 472-73 (1988).

46. See discussion *supra* note 21.

consumers, particularly the more marginal ones, would be shut out of the credit card market and, in the final analysis, would neither appreciate, nor benefit from, the government's paternalistic "consumer protection" of interest rate caps.<sup>47</sup> Consumers would benefit not from protectionist laws that stifle economic growth and limit individual choice, but rather from better information with which to educate themselves about available credit options. Such information would enable them to make rational credit decisions based on their particular needs.<sup>48</sup>

Ultimately, this second contention, which I will call the "free-market argument," is the most important. The argument essentially has two parts. The first part employs the language of liberal market economic theory by suggesting that the most efficient markets are those that most closely resemble "perfect competition" and are allowed to operate free from "artificial" restrictions, such as government regulation.<sup>49</sup> Interest rate controls introduce a distortion into a market that would otherwise operate in a naturally competitive way. The second part of the argument draws on traditional American ideas about freedom and individualism to support the view that consumers should be able to go into the market and make bargains for credit as they see fit. The government should not interfere by imposing an

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47. In 1987, in a statement opposing any federal cap on credit card interest rates, Federal Reserve Board Governor Martha Seger said that the Federal Reserve opposed any attempts to cap interest rates because it "would likely reduce the amount of credit made available, forcing consumers to rely instead on less convenient and possibly more expensive substitutes, or to lose access to credit at any rate." *Fed Opposes Legal Cap on Credit Card Interest Rates*, L.A. TIMES, April 22, 1987, §4, at 3. Seger added that this burden would fall most heavily on lower-income borrowers and perhaps would lead to increases in other credit card charges, such as annual fees and processing charges. *Id.*

48. This information is essentially what consumers now receive after the 1988 legislation. See *supra* note 36 and accompanying text.

49. Markets in perfect competition have the following attributes: (1) numerous buyers and sellers; (2) a quantity of goods such that no single buyer or seller perceives that he or she can affect price by varying the quantity demanded or supplied; (3) product homogeneity; (4) accurate and complete product information for buyers and sellers; and (5) freedom of entry into and exit from the marketplace. SIDNEY SHAPIRO & JOSEPH TOMAIN, *REGULATORY LAW AND POLICY* 181 (1993).

Under these strict conditions, a market attains its virtues by moving toward equilibrium, where the proper amount of goods are placed on the market at the proper prices. If any one of these conditions is missing, the market is imperfect. In other words, a market failure exists, and government regulation may be needed to correct that failure.

*Id.* Perfect competition is, however, an idealized version of the marketplace; no market is perfectly competitive. *Id.* at 189.

artificial limit on the types of deals that can be made, particularly when such a limitation would mean that certain people would be unable to make deals at all. Most arguments against regulation of credit card interest rates have been built upon these two themes—hence the contentions by opponents of interest rate controls that greater access to information would produce a more “rational” market, that consumers as a whole would be hurt if credit cards were more expensive and available to fewer people, and that “tighter” credit would have negative consequences for the country’s economic well-being because it would make it more difficult for people to spend money. Opponents of credit card interest regulation employ this free-market argument liberally, and the presumptions underlying it are not often discussed.<sup>50</sup>

Regardless of the ultimate merits of the credit card industry’s explanation for high credit card interest, an explanation that I will examine in more detail below, it is clear that despite high rates, the credit card business has expanded dramatically and card issuers continue aggressively to court, and win, new customers.<sup>51</sup> The business is extremely profitable and many customers are clearly willing to pay a substantial premium in order to have access to the bundle of services that credit cards

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50. A complete review of all of the circumstances in which this argument has been used would be impossible. It appears in most major debates on controlling credit card interest rates. Sources as important as the Federal Reserve have relied on it, see *Fed Opposes Legal Cap on Credit Card Interest Rates* (comments of Federal Reserve Governor Martha Seger), *supra* note 47, as have the *New York Times* and other major newspapers. In an editorial opposing federally mandated rate caps in 1991, the *Times* stated that “[m]illions of cardholders would suffer, because banks and other issuers would cancel the cards of less credit worthy customers. People with limited incomes would suffer most; they depend on the elbow room a credit card provides.” *The Senate’s Credit Card Blunder*, N.Y. TIMES, Nov. 20, 1991, at A26. In addition, an editorial in the *Los Angeles Times* noted:

The populist appeal of lower credit card rates is undeniable. But to legislate such a move now would be a disaster both for consumers and the already fragile banking industry. Capping rates now would force banks to scale back on issuing credit cards. That could make credit less available to hard-pressed consumers who sometimes use their cards to survive.

*Cut Credit Card Rates? Careful How You Do It; Offering Political Lollipops Won’t Improve the Economy*, L.A. TIMES, Nov. 19, 1991, at B6.

51. In 1993, bank card issuers had their most profitable year since 1990, despite the introduction of some lower rate cards and increased competition from new entrants into the credit card market such as Ford and General Motors. *Competition: The Credit Card Industry Rides a Wave of Profitability*, *supra* note 17. Credit card profits continued to rise in 1994, with Visa and MasterCard issuers earning after-tax profits of \$4.7 billion, up 4.4% from 1993. *Id.* Profit margins declined slightly from a 2.3% after tax return on assets in 1993 to a 2.1% return in 1994. *Id.*



provide. Why should the law intervene when the market has established a price for a service that consumers want and that credit card issuers are eager to offer?

## II. THE ECONOMIC ARGUMENTS SURROUNDING REGULATION OF CREDIT CARD INTEREST RATES

### A. *The Economic Argument Against Regulation*

From an economic perspective, interest is the cost to a borrower for the use of money over a specified period of time. The actual interest rate charged will reflect several factors, including (1) the relationship between the supply and demand for credit in the relevant market, (2) the element of uncertainty of repayment, or risk of default, which will vary with the type of loan and borrower, and (3) the perceived cost of "riskless" credit.<sup>52</sup> These factors together will create a "market" rate of interest. When a usury ceiling exists, market forces will determine the cost of credit as long as the market rate does not exceed the legal rate. If, however, the market rate is higher than the legal rate, lenders have no economic incentive to lend because the legal rate produces insufficient profit relative to the costs and risks of making loans. Lenders will decline to make loans at the legal rate and will look instead for investments that will earn a market rate of return.<sup>53</sup> Consequently, there will be less credit available in the market affected by the usury statute, thus inhibiting the ability of consumers to express their preferences for goods in the economy with money. The prices and terms of the credit that is available will often be more restrictive because lenders will compensate for their inability to charge a market interest rate by lending to consumers who offer lower risk and by increasing costs related to borrowing that are not considered under the law to be interest, such as down payments, processing fees, and collateral requirements. These changes in the market will tend to fall most heavily upon those consumers with lower incomes because they are generally perceived by lenders as posing a higher risk of default, wanting smaller loans (which are less profitable when costs are high), being unable to pay increased fees, and being less

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52. Note, *Usury Legislation: Its Effects on the Economy and a Proposal for Reform*, 33 VAND. L. REV. 199, 212 (1980).

53. *Id.* at 212-13.

likely to have collateral.<sup>54</sup> Thus, from the perspective of liberal economic analysis, usury laws are counterproductive because they constrict the supply of credit in the economy and the ability of consumers of credit to make economic choices. Such laws hurt the poorer members of society because they are the least likely to get credit when usury law ceilings are below market rates. If one assumes that a major purpose of usury laws is to protect lower income borrowers, then the economic analysis suggests that the laws harm exactly those people they are supposed to help.<sup>55</sup>

Notwithstanding the impressive lobbying efforts of the credit card industry, congressional reluctance to impose caps stems from more than special-interest politics. It is also rooted in the very terms of the debate; in other words, in the construction of the arguments against interest rate regulation primarily in the language of liberal economics and individualism. The arguments in support of interest rate regulation, or usury laws, have a strong moral tone. These arguments are often seen as illegitimate justifications for legal policy in a liberal democratic state.<sup>56</sup> Furthermore, how one manages credit card debt is an individual

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54. *Id.* at 214. But see George J. Wallace, *The Uses of Usury: Low Rate Ceilings Reexamined*, 56 B.U. L. REV. 451 (1976). Wallace accepts this argument, but comes to a different conclusion about what it means. He contends that interest rate ceilings that have the effect of denying credit to high-risk borrowers may be justifiable on the grounds that they protect those consumers from a product that could be particularly dangerous to them. *Id.* at 458.

55. The economic effects of interest rate controls on the credit card market during the early 1980s were analyzed by Christopher C. DeMuth in *The Case Against Interest Rate Controls in the Credit Card Market*, 3 YALE J. ON REG. 201 (1986). DeMuth argues that price controls in the form of usury laws in the credit card market generally leave consumers less well off by causing the supply of credit to grow more slowly or by creating undesirable changes in the terms and manner in which credit is provided. *Id.* at 221. He determines that a national rate ceiling for credit cards would decrease the availability of credit cards for those who are considered higher credit risks and would increase forms of credit that were unregulated, more costly, or both. *Id.* at 237-42.

56. Ronald Dworkin writes that liberalism takes as its constitutive morality the theory that political decisions must be independent of any particular view of what constitutes the "good life"; in other words, what gives value to life. Ronald Dworkin, *LIBERALISM, excerpted in LIBERALISM AND ITS CRITICS* 60, 63-65 (Michael Sandel ed., 1984). See also JOHN RAWLS, *POLITICAL LIBERALISM* (1993). Rawls writes, "[p]olitical liberalism assumes that, for political purposes, a plurality of reasonable yet incompatible comprehensive [religious, philosophical, and moral] doctrines is the normal result of the exercise of human reason within the framework of the free institutions of a constitutional democratic regime." *Id.* at xvi. In *Political Liberalism*, Rawls reconsiders this foundational concept of liberalism, a concept that formed an important part of his seminal work on liberal theory, *A THEORY OF JUSTICE* (1971).

problem or choice. One may make unwise or even irresponsible decisions, but Congress is unwilling to prevent people from exercising their "right" to do so.<sup>57</sup> The concerns that inspired usury laws over centuries of human history may still be relevant to the discussion, but as moral ideas, they are too value-laden to compete with positions grounded in the culturally neutral, individually oriented "rights talk" of the opponents.<sup>58</sup>

A more complete rationale for why federal interest rate controls have not been imposed on the credit card market emerges when one considers the interest-group theory of regulation, which suggests that the creation of law and public policy results from the struggles of interest groups to redistribute wealth in their favor.<sup>59</sup> Thus, "legislatures pass laws to benefit those groups that are able to pay for the laws with promised political support. The costs of these laws are borne by those who are in the worst position to object to them—the amorphous and disaggregated public."<sup>60</sup> Deregulation of financial services reached its zenith during the period when the combination of high interest rates and restrictive usury laws were cutting deeply into the banking industry's profits. The removal of usury restrictions in the credit card market ushered in a new era of extraordinary profitability for consumer lending, which continues to this day. Legislative action to limit interest rates would cap the growth in profits. Credit card issuers have a strong incentive to lobby Congress to prevent the passage of any type of interest rate regulation. By casting the debate over controlling interest rates in terms of the individual's freedom to choose and by threatening to deny access to credit, they have been able to confound the

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57. Liberal economic theory is well suited to the American obsession with characterizing personal choices in terms of rights. For a discussion of the American fascination with individual rights and its effects on the discussion of social and political issues in the United States, see generally MARY ANN GLENDON, *RIGHTS TALK* (1991). By stressing individual autonomy and personal freedom to choose, opponents of interest rate caps can often deflect attempts to "restrict" choices. Glendon notes that "[o]ur rights laden public discourse easily accommodates the economic, the immediate, and the personal dimensions of a problem, while it regularly neglects the moral, the long-term, and the social implications." *Id.* at 171.

58. See generally *id.*

59. Richard A. Posner, *Economics, Politics, and the Reading of Statutes and the Constitution*, 49 U. CHI. L. REV. 263, 265 (1982).

60. Jonathan R. Macey, *The Myth of "Reregulation": The Interest Group Dynamics of Regulatory Change in the Financial Services Industry*, 45 WASH. & LEE L. REV. 1275, 1278 (1988).

opposition. Any attempt to examine the broader ramifications of lack of interest rate controls in this market tends to devolve into an argument about freedom of choice and the benefits of the free market. Thus this transfer of wealth from American consumers to the credit card industry has been met by no effective congressional response.

The free-market argument has provided a strong defense against congressional attempts to regulate credit card interest rates at the national level. Credit, whatever its cost, is seen as beneficial, and it is more beneficial when it is available to the largest possible number of people. Certainly credit makes it easier for people to purchase all kinds of goods and services, and, as was discussed above, the American economy is quite dependent on consumer spending; as a result, encouraging consumption benefits the innumerable businesses that depend on consumer credit to remain profitable.<sup>61</sup> No one wants to be responsible for taking away credit from the poor or other risky debtors and curtailing their ability to consume. Yet despite the widespread use and acceptance of the free-market argument, it has not gone unchallenged.

#### *B. Problems with the Economic Argument Against Regulation*

In *The Failure of Competition in the Credit Card Market*,<sup>62</sup> Lawrence Ausubel takes issue with some of the basic assumptions that are essential to the economic foundation of the free-market argument. Ausubel asserts that, despite the large number of participants and the lack of significant regulatory controls, the assumption that the credit card market in the 1980s would reflect a competitive market model is empirically unjustified. To support this contention, he finds that consumer behavior in the credit card market is economically irrational and that consumers are particularly insensitive to changes in interest rates.<sup>63</sup> Further-

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61. See, e.g., Robin A. Morris, *Consumer Debt and Usury: A New Rationale for Usury*, 15 PEPP. L. REV. 151, 169 (1988) ("Today, institutional pressures to increase consumer debt outweigh borrower incentive to refrain from indebtedness. Lenders, pushed by new competition from any business that has enough market power to raise and lend money, are under enormous pressure to sell credit and expand their portion of consumer debt in order to maintain profits.")

62. Ausubel, *supra* note 17.

63. *Id.* at 71-72.

more, he determines that the rates of return for the credit card business are three to five times what is ordinarily seen in other areas of the banking industry.<sup>64</sup> Irrational consumer behavior and "supranormal" profits do not suggest an industry operating in a model of intense competition.<sup>65</sup>

Ausubel reviews the profit figures for the fifty largest credit card issuers in the United States and does a detailed analysis of the revenues and costs of one issuer that was fairly typical of the group, Maryland Bank, N.A. ("MBNA").<sup>66</sup> His analysis reveals that the single largest component of MBNA's revenue is finance charges and that, despite a twenty-five day grace period on outstanding balances, fully eighty percent of MBNA's credit card accounts incurred such charges.<sup>67</sup> In 1987, MBNA's after tax return on assets in its credit card division was 2.78 % (4.8 % before taxes), which compared to a return after taxes of one percent for the holding company as a whole.<sup>68</sup> Ausubel concludes, after examining the returns of several other major card issuers, that credit cards generally earn three to five times the ordinary

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64. *Id.* at 63-64.

65. "Supranormal" is Ausubel's description of the credit card profits he documented during his study period. *Id.* at 50. Rather than suggesting that firms are competing in a market approaching perfect competition, which has been the argument of credit card issuers and opponents of interest rate regulation, high profits and the entrance of many new suppliers of a product into a market tend to indicate the existence of a market in monopolistic competition. RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 124-25 (4th ed. 1992). When prices exceed competitive levels in an industry, producers can lower prices or they can engage in nonprice competition by offering better service, higher quality, or incentives to use the product. *Id.* at 278-79. See also MANDELL, *supra* note 6, at 80-81. In the most recent comprehensive government report on the credit card industry, the General Accounting Office was unwilling to confirm or reject the contention that the credit card market functions in an anticompetitive manner. GAO REPORT, *supra* note 4, at 24.

66. MBNA was the thirty-ninth largest U. S. bank holding company at the time of Ausubel's study and the seventh largest issuer of MasterCard and VISA cards. Ausubel, *supra* note 17, at 52. Ausubel notes that MBNA was founded in 1982 in Newark, Delaware, "apparently to avoid Maryland's usury law." *Id.* at 57 n.18. In 1993, MBNA was the fourth largest issuer of credit cards in the nation. *Top 50 Companies in Bank Credit Card Lending*, THE AMERICAN BANKER, Sept. 20, 1993, at 20.

67. Ausubel, *supra* note 17, at 58. Ausubel notes in a footnote on the same page that a good rule of thumb mentioned in credit card trade publications is that 90% of a card issuer's outstanding balances will incur interest charges. *Id.* at 58 n.20.

68. *Id.* at 59. MBNA's return on assets in 1987 was very close to the industry averages for 1992 and 1993, which were 2.0% and 2.3% respectively. *Competition: The Card Industry Rides a Wave of Profitability*, *supra* note 17.

rate of return in the banking industry.<sup>69</sup> Thus, the returns in this business appear to justify whatever costs that must be incurred. Ausubel correctly predicted that high profits would be maintained in the years 1990-93.<sup>70</sup>

Ausubel also finds substantial variance with competitive-market theory when he examines the behavior of credit card consumers. The percentage of accounts incurring interest charges is substantially higher than the percentage of consumers who say they carry balances, and Ausubel surmises that most consumers are unwilling to admit, or are even unaware of, how often they borrow money by using credit cards.<sup>71</sup> Furthermore, consumers are much more sensitive to increases in annual fees than they are to increases in interest rates.<sup>72</sup> He sees consumer behavior in the credit card market as irrational and states that the "proclivity of consumers to borrow at these high rates suggests a substantial breakdown in optimizing behavior among credit card holders."<sup>73</sup> Ausubel does not suggest that his findings lead to the conclusion that credit card interest rates should be capped. He argues, however, that it is flawed reasoning from a regulatory standpoint to support the present laissez-faire interest rate regime in the credit card market by using arguments drawn from a model of perfect competition.<sup>74</sup> Neither the behavior of consumers, nor the

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69. Ausubel, *supra* note 17, at 63-64. Ausubel determines that the ordinary (pretax) return on equity in banking was around 20% during the period 1983-88 and that credit cards earned returns of 60% to 100% during the same period. *Id.*

70. See *Banking Industry Reaps Credit Card Profits*, *supra* note 17.

71. Ausubel, *supra* note 17, at 71-72.

72. *Id.*

73. *Id.*

74. *Id.* at 74. Indeed, there is increasing evidence that more economists are recognizing the substantial flaws contained in models of "economic rationality." On attempts by economists to encompass a more realistic view of the way people think in economic models, see *Rational Economic Man: The Human Factor*, THE ECONOMIST, Dec. 24, 1994, at 90.

Professor Ausubel recently completed a follow-up study on the credit card market. Lawrence Ausubel, *The Credit Card Market: Revisited* (July 20, 1995) (unpublished manuscript, on file with the *University of Colorado Law Review*). After reviewing a wider sample of market data from the credit card market from 1971 through 1993, Ausubel was able to confirm his earlier finding that the credit card market does not conform to a market model of perfect competition. *Id.* at 2. He reports that although interest rate "stickiness" has declined during the 1990s, the return on assets for credit cards from 1983 to 1993 has averaged five times the return on assets for the entire banking system. *Id.* Additionally, Ausubel extends the empirical investigation of the phenomenon of consumer underestimation of the amount borrowed on credit cards and finds that consumers underestimate or underreport their credit card balances by a factor of two. *Id.* at 3. Indeed, Ausubel

behavior of suppliers of credit, indicates the existence of a competitive or rational market.

Ausubel's arguments cast doubt on the ability of free-market economic theory to provide an adequate justification for a legal policy that rejects interest rate controls in the credit card market based in large part on putative benefits to consumers due to the increased availability of credit in an "unregulated" market. When profits are examined, card issuers are certainly major beneficiaries of the current policy, and this fact no doubt accounts for its endurance. What one can conclude from the economic analyses, and from the statistical information available, is that an unregulated interest rate regime in the credit card market will have several important results. First, there will be a large supply of credit available to a broad spectrum, in socioeconomic terms, of the population. Second, this credit will be extremely expensive relative to other modes of borrowing. Third, the overwhelming majority of people who have access to this credit will borrow, despite the high cost. Fourth, the cost to card issuers of providing credit cards will be money well spent given the return on the investment. Money directed into credit card operations will reap a larger return than it would if directed into other types of lending. The cost argument should thus be rejected as a satisfactory explanation for high credit card interest rates.

Considering traditional free-market economic reasoning when selecting a legal rule, particularly when the subject is interest rate regulation, is an important part of determining whether the rule is sound. But it is only a part of such a determination. Without a broader inquiry, this consideration alone may lead to the acceptance of rules that, while perhaps appropriate in the theoretical marketplace, create disturbing problems in the real world.<sup>75</sup> Banks and other businesses do not issue credit cards

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notes that this "underestimation hypothesis" was seen as "the key provocative and ideological issue" of his work by some readers and, although he is somewhat uncomfortable with a behavior theory that varies so widely from that which is generally assumed by economists, he admits that it "does genuinely appear to ring true." *Id.* at 1.

75. Professor Kripke has expressed concern about the increasing reliance on abstract economic theories and secondary sources to gain an understanding of the business world; he advocates, instead, greater use of "realistic observation" of what actually happens. Homer Kripke, *Law and Economics: Measuring the Economic Efficiency of Commercial Law in a Vacuum of Fact*, 133 U. PA. L. REV. 929, 932-33 (1985).

hoping that people will immediately pay their debts. The "convenience user" who never incurs an interest rate charge is the bane of the credit card issuer's existence.<sup>76</sup> Credit card issuers must assume that most consumers will go into debt when they have credit cards in their pockets and that these debts will be paid off over time.<sup>77</sup> They depend on this to make high profits. From a social policy perspective, it does not seem particularly remarkable that many people behave irrationally when they have access to the "easy money" that credit cards provide. There has probably been no other time in American history when such a large cross section of the population has had access to so much money and at the same time had almost unlimited spending opportunities.

Are we better off as a social community when our impulse to spend money that we do not have is constantly encouraged? By allowing us to consume fairly painlessly, credit cards mask the hard, cold reality that most of us cannot afford all of the things we want, and many of us cannot afford all of the things we need. This is the broad issue with which the law must be concerned, and to analyze it exclusively in the language of liberal economic market theory is inappropriate. By limiting the discussion to the language of the market we have limited our understanding of human nature and the role of the law to the acquisitive and rational values of the commercial economy, despite the fact that

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76. If a card has a grace period, the convenience user gets an interest free loan from the time the purchase is made until the time that payment is due. The credit card industry has begun to discuss ways to make convenience users pay for the "privilege" of having a credit card, such as charging transaction fees, shortening grace periods, and tying perks such as low interest rates and rebates to the amount of debt a customer carries. Glenn Burkins, *Banks Target Paid-Up Cards: "Convenience Users" Eat Into Profits*, ARIZ. REPUBLIC, June 28, 1993, at E3.

77. Since 1980, the delinquency rate (more than thirty days past due) for bank card loans has generally averaged between 2% and 3%. STATISTICAL ABSTRACT, *supra* note 3, at 522. Thus, in a bad year, 97% of the accounts are current. Professor Warren has noted:

Banks have rising losses in consumer bankruptcy, but what have they done every single year? They have put out as many more cards as they could. Why? Because it is profitable to take those credit card losses. That is what the statistics show them: go ahead, because although one out of a hundred debtors cannot pay, 99 are paying off at 21% interest. And when the spread between the wholesale and retail cost of money is from 6% to 21%, business is profitable—even the highest risk business.

Warren, *supra* note 4, at 1108.



our communal, real-world experience tells us that economic exchange is not always the driving force behind our choices.<sup>78</sup>

### III. CONSTRUCTING A RICHER UNDERSTANDING OF THE ROLE OF INTEREST RATE CONTROLS IN THE CREDIT CARD MARKET

#### A. *Coming to Terms with the Concept of Usury*

It is impossible to evaluate the current lack of interest rate controls in the credit card market without placing the issue in the context of the long-standing debate surrounding usury laws. There are few forms of economic regulation that have a more ancient lineage than the laws against usury. In the Western legal tradition,<sup>79</sup> laws prohibiting the lending of money for a profit were found among the Greeks and the Romans and were also part of ancient Jewish law.<sup>80</sup> In the medieval Christian world, the taking of interest on money was seen as an affront to the universal brotherhood of man and was strongly condemned as immoral.<sup>81</sup> Traditionally, prohibitions against usury in the Western tradition were grounded in the Aristotelian idea, later promoted by Christian thinkers, that the purpose of money was exchange. It could be traded for another good, but its basic nature was sterile, and it could not reproduce itself. In other

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78. I am borrowing a theme here from James Boyd White, which he discussed in his essay, *Economics and the Law: Two Cultures in Tension*, 54 TENN. L. REV. 161, 194-96 (1987).

79. For the purposes of this article, the "Western legal tradition" encompasses those legal systems that draw their primary inspiration from Greek, Roman, and Hebrew texts and the experience of Christianity. See HAROLD J. BERMAN, *LAW AND REVOLUTION: THE FORMATION OF THE WESTERN LEGAL TRADITION* 1-10 (1983). Although there are different ways of specifying the systems, there is general agreement that this would include the Anglo-American and Romano-Germanic legal systems that predominate in North and South America, the British Isles, and the European continent. *Id.*

80. In ancient law, usury was generally defined as the taking of any profit upon a loan of money. Aristotle wrote in condemnation of usury. ARISTOTLE, *THE POLITICS*, Book 1, Ch. 10 (Carnes Lord trans., 1984). See also ODD LANGHOLM, *THE ARISTOTELIAN ANALYSIS OF USURY* (1984). The Romans limited the taking of interest in the Law of the Twelve Tables (449 B.C.). JEAN-PHILIPPE LEVY, *THE ECONOMIC LIFE OF THE ANCIENT WORLD* 55 (1967). The Jews were forbidden by Moses to practice usury among themselves. *Leviticus* 25:35-37.

81. Both Albertus Magnus and Thomas Aquinas condemned usury as sinful, evil, and contrary to ideas of Christian brotherhood espoused in the Gospels. BENJAMIN NELSON, *THE IDEA OF USURY: FROM TRIBAL BROTHERHOOD TO UNIVERSAL OTHERHOOD* 13-14 (1969).

words, it was contrary to the ways of nature for money to produce more money.<sup>82</sup> Usury was thus an act contrary to the laws of nature and, eventually, God's law. As capitalism grew in Europe, however, the prohibition against usury became more tempered. The abstract natural-law argument became increasingly difficult to square with Europe's growing commercial needs, and eventually "usury" came to be understood as the lending of money above the legal rate set by the sovereign.<sup>83</sup> It is unlikely, however, that the natural law argument was the foundation upon which the prohibition against usury was built.<sup>84</sup>

Societies have recognized throughout recorded history that people burdened with excessive debt are prime candidates for exploitation; civil and religious leaders in all parts of the world have assumed that laws regulating the taking of interest were necessary. Most usury prohibitions are grounded in deep ethical and religious condemnations of the exploitation of the weak, of socially destabilizing concentrations of wealth, and of the accumulation of money or wealth without an investment of labor.<sup>85</sup> John Noonan argues that "the vitality and relevance of

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82. In Aristotle's view:

[U]sury is most reasonably hated, because one's possessions derive from money itself and not from that for which it was supplied. For it came into being for the sake of exchange, but interest actually creates more of it . . . .  
[I]nterest is money born of money. So of the sorts of business this is the most contrary to nature.

ARISTOTLE, *supra* note 80, at 49-50. See also John T. Noonan, Jr., *Tokos and Atokion: An Examination of Natural Law Reasoning Against Usury and Against Contraception*, 10 NAT. L. F. 215, 16-219 (1968).

83. The Protestant countries were the first to break with the traditional prohibitions against usury in Europe, and John Calvin was the first major religious leader to legitimate, from a Christian perspective, the taking of interest. NELSON, *supra* note 81, at 73-78. But Calvin saw important limitations: An excessive rate was always objectionable, it was sinful constantly to accept usury, and it was impermissible to take usury from the poor. *Id.* The general rule was that usury was permissible if it was not injurious. *Id.* This view eventually established itself in England and the American colonies. *Id.* at 95; Raymond B. McConlogue, *Usury*, 1 S. CAL. L. REV. 253, 255-56 (1928).

84. Noonan, *supra* note 82, at 222.

85. The traditional hostility to usury is found in societies around the world, including India, China, and all the Islamic countries. 2 FERNAND BRAUDEL, *CIVILIZATION AND CAPITALISM 15TH-18TH CENTURY: THE WHEELS OF COMMERCE* 561 (Siân Reynolds trans., Harper & Row 1982) (1979). The traditional Islamic view, still widely accepted by many Moslems today, rejects the taking of interest on three major grounds:

(1) Interest or usury [excessive interest] reinforces the tendency for wealth to accumulate in the hands of the few, and thereby diminishes man's concern for his fellow man[.]

the [usury] rule are not to be identified with the supporting rationale of the nature of money. The rule protected certain values," Noonan notes, "not the rule itself and not the argument based on nature—which were to prove to be permanent parts of the Christian tradition."<sup>86</sup>

In the Christian tradition, three major arguments were advanced in support of usury prohibitions—usury is uncharitable, it breeds the sin of avarice, and it has undesirable social consequences.<sup>87</sup> Simply put, usury was seen as a moral evil in society, and a rule of general application was needed to address its consequences. Noonan argues that it was the attempt to rationalize the rule through the "nature of money" argument that invited subsequent modifications of the usury prohibition in the Christian world.<sup>88</sup> The endurance of usury laws through the centuries and throughout the world is an ongoing attempt by societies to grapple with specific moral issues in human and economic relations.

In the United States, usury statutes traditionally have been the province of state law.<sup>89</sup> Over the last twenty-five years, however, a majority of lawmakers have come to believe that laws limiting an individual's right to negotiate the terms of a loan are economically inefficient and unacceptably "paternalistic." As an example of this change, Congress has intervened on various occasions to override state usury laws; in addition, many state legislatures have had little difficulty liberalizing or abandoning

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(2) Islam does not allow gain from financial activity unless the beneficiary is also subject to the risk of potential loss; the legal guarantee of at least nominal interest would be viewed as guaranteed gain; and]

(3) Islam regards the accumulation of wealth through interest as selfish compared with accumulation through hard work and personal activity.

Talib Siraaj Abdus-Shahid, *Interest, Usury, and the Islamic Development Bank: Alternative, Non-Interest Financing*, 16 LAW & POL'Y INT'L BUS. 1095, 1102-03 (1984).

86. Noonan, *supra* note 82, at 222.

87. *Id.*

88. *Id.* at 225.

It was a moral rule binding all men in the society because usury was a real evil in the society. The reality of that evil was expressed in an argument which now seems clumsy . . . Its actual function was not to convince, but to symbolize. . . . But putting the case against usury on a rational level it invited all the subsequent changes.

*Id.*

89. For a general discussion of the development of state usury laws in the United States, see James M. Ackerman, *Interest Rates and the Law: A History of Usury*, 1981 ARIZ. ST. L.J. 61.

their usury laws in order to promote the growth of credit markets and local financial-services businesses.<sup>90</sup>

*B. Crafting a Broader Perspective on the Role of Interest Rate Controls in the Legal System*

By relying on the language of market economics, the opponents of interest rate controls for credit cards have been able to make their case in terms that are accepted increasingly in our social and political discourse as neutral. Opponents of interest rate controls are characterized as reasoned promoters of efficient markets and freedom of choice, whereas the proponents tend to be seen as moralizers or naive populists. The proponents' attempts to talk about questions such as issuer greed, excessive profits, and consumer weakness come across as hopelessly rooted in "values" and paternalism, and therefore undeserving of serious consideration in the public sphere.<sup>91</sup> The idea that the market is one of the few institutions neutral enough to accommodate the varying needs and goals of a diverse society has become difficult to contest in American public life.

James Boyd White wrote of the dangers of accepting the language of market economics as the rhetoric for our communal discourse on law and public policy.

It is not too much to say, I think, that the modern celebration of the market as the central social institution—the most fair, the most respecting of autonomy, and the most efficient—threatens to destroy the single greatest achievement of Western political culture: the discovery that a community can govern itself through a rule of law that attempts to create a fundamental moral and political equality among human beings.<sup>92</sup>

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90. See *supra* note 31 and accompanying text. In 1980, Congress preempted state usury regulations as they applied to first mortgage loans on homes in Title V of the Depository Institutions Deregulation and Monetary Control Act, at 12 U.S.C. § 1735f-7a (1994).

91. For an example of the hostility of liberal political theory to moral claims generated by religious tradition, see STEPHEN L. CARTER, *THE CULTURE OF DISBELIEF* 224-26 (1993).

92. White, *supra* note 78, at 183. See also ROBERT N. BELLAH ET AL., *THE GOOD SOCIETY* 82-110 (1991).

Liberal economics, White notes, assumes that individuals are rational economic actors, "without race, gender, age, or culture,"<sup>93</sup> who are motivated primarily by the desire to consume and acquire. Most economists do not suggest that this is a completely true representation of the way people always behave, only that it is a helpful simplification that serves as a reliable predictor of behavior, and that it is probably more reliable than any alternative hypothetical model. But White argues that as one becomes steeped in the language and the methods of liberal economics, it becomes impossible to remain objective as to the merits of this explanation of how the world works. Thus, most economists really do believe that the system tells the truth about the world.<sup>94</sup> This happens not only to economists, but also to noneconomists who speak the economic language.

The language of economics takes terms such as "self-interested" and "rational" and applies them to human behavior in a technical, market-oriented sense. Any negative or unrealistic connotations the words have when applied to human behavior in their ordinary way are disregarded for the purpose of economic analysis. White contends:

[O]ne cannot habitually think of human action in such terms—especially in a culture like our own, which is so heavily dominated by the motive of self-interest in the usual sense . . . without in fact universalizing the ordinary rather than the technical meaning. The result is to validate both selfishness and the desire to acquire and consume.<sup>95</sup>

The language of economics is offered to the law as the language on which legal analysis should proceed and to the public at large as a way to explain our communal life. Although the system claims to be value-neutral, it tends to make rational self-interest central and habituates the individual to thinking in those terms. Furthermore, the value neutrality that the system claims is troubling in its own right, for it tends to remain silent on

all questions of value that are external to the acquisitive and competitive ones enacted in the exchange game . . . . But this is to be silent on all the great questions of human life: ques-

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93. White, *supra* note 78, at 168.

94. *Id.* at 169-70.

95. *Id.* at 171.

tions of beauty and ugliness in art and music, sincerity and falsity in human relations, wisdom and folly in conduct and judgment, and the greatest of all questions, which is how we ought to lead our lives.<sup>96</sup>

In White's view, the language and culture of the law must be broad enough to encompass those "great questions," and it cannot be allowed to collapse into the economic mode of thought. In other words, the market must be subordinated to the values and practices of our larger culture.<sup>97</sup>

As if justifying White's concerns, the public discussion of the issue of credit card interest rates indicates that the language of economics has become the language of law and public policy. Having asserted that a free market for credit is beneficial to society because more people will have access to credit (and thus will have access to the marketplace) and that interest rate controls are detrimental because they will take credit away from people (thus making market participation more difficult and denying them freedom of choice), the opponents of interest rate controls essentially rest their case. In a culture where the ability to consume and acquire is central to achieving happiness and satisfaction, such an argument might be sufficient. Although one could argue that this indeed describes the core of the American cultural experience, there is some hopeful evidence to the contrary. Our actions are not driven by market values alone. Certain cultural concerns have remained constant in society's struggle with the concept of usury laws, two of which are particularly relevant to this discussion: (1) discouraging avarice and promoting charity, and (2) protecting the economically weak from exploitation by the economically powerful.<sup>98</sup> Despite the tendency

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96. *Id.* at 174. This is, in essence, a critique of Dworkin's central theory of the liberal state. See discussion *supra* note 56.

97. White, *supra* note 78, at 197. White also notes that he is not opposed to the continuation of the market economy, but he favors it on the pragmatic ground that there is no better alternative. Its results are not "entitled to any special veneration or respect if they seem . . . on independent grounds to be undesirable." *Id.* at 197 n.35.

98. In their pastoral letters on Catholic social teaching, politics, and the U.S. economy, the U.S. Catholic bishops have spoken extensively on these topics, urging a more just distribution of wealth, equal human dignity of all persons in economic transactions, and respect for the dignity of work. See NATIONAL CONFERENCE OF CATHOLIC BISHOPS, ECONOMIC JUSTICE FOR ALL (1986). Similar concerns are pervasive in Islamic thought as well. See discussion *supra* note 85. In the Jewish tradition, the right to acquire property and wealth has always been subordinate to

for these ideas to be overlooked in public discussions of interest rate regulation, they continue to resonate throughout American culture and are quite relevant to any discussion of the credit card market.

### 1. The Problem of Greed

Aristotle condemned the acquisition of wealth for wealth's sake as unnecessary and potentially unlimited.<sup>99</sup> In the United States, there is a historical distrust of banks and the banking industry that can be traced to the earliest days of the republic.<sup>100</sup> This distrust is based in large part on the huge amounts of capital amassed by banking institutions and how those institutions have tended to exercise undue influence over the political and economic system. Today, this concern is often dismissed as so much populist nonsense, but the 1980s showed that the general public is wise to be suspicious.<sup>101</sup> The federal government, and consequently the nation's taxpayers, have borne huge costs as a result of banking deregulation.<sup>102</sup>

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concerns about the quality of human life. ALBERT VORSPAN & EUGENE J. LIPMAN, *JUSTICE AND JUDAISM* 186-87 (1956).

99. ARISTOTLE, *supra* note 80, at Book 1, Ch. 9.

100. The struggle between Thomas Jefferson and Alexander Hamilton over the First Bank of the United States set the stage for two centuries of conflict over the role of large banks in American society. Hamilton saw a large central bank as essential to the young nation's developing commercial economy and feared the lack of strong central authority, while Jefferson saw concentrated power as inherently dangerous and favored a decentralized, agrarian society. *See, e.g.*, BELLAH ET AL., *supra* note 92, at 68-70.

101. A common way to dismiss concerns about accumulation of wealth in the banking industry is to call them "populist," which tends to conjure up images of unsophisticated farmers or flamboyant politicians from the late 19th and early 20th centuries. *See* Lawrence J. White, *The Community Reinvestment Act: Good Intentions Headed in the Wrong Direction*, 20 *FORDHAM URB. L.J.* 281, 281 (1993) ("The heavy hand of nineteenth century populism continues to have a powerful effect on late twentieth century banking policy in the United States."). Any notion current among the "people" concerning the dangers of concentrated wealth were vindicated when, after exacting all kinds of deregulatory concessions from Congress in the late 1970s and early 1980s, the banking and savings and loan industry dragged the nation through the worst financial crisis in fifty years. On the problems of the American bank regulatory system and how those problems might be repaired, see generally HELEN A. GARTEN, *WHY BANK REGULATION FAILED* (1991).

102. The cost to the American taxpayers of the financial crises of the 1980s has been estimated at \$157 billion over the next thirty-three years. Jeryl Bowers, Comment, *The Resolution Trust Corporation's Override Regulation: Freedom For Intrastate Branch Banking*, 59 *U. CHI. L. REV.* 691, 691 (1992).

The recent history of the credit card industry demonstrates yet another large transfer of wealth to the financial services industry, although this time it comes directly from consumers. Nonetheless, there is very little acceptable public language to discuss explicitly what many people believe implicitly—that credit card issuers have been taking advantage of consumers to a degree that is at best unseemly and at worst unconscionable.<sup>103</sup> Such a belief suggests a value standard by which the conduct of credit card issuers can be judged and that, at a certain level or under certain conditions, there is a point where profits become excessive. The value assumption makes it difficult to express these ideas in a public forum and have them discussed in any serious way.<sup>104</sup> When Senator Alphonse D'Amato introduced legislation to cap credit card rates in 1991, he stated that bank profits on credit cards were unreasonable and that card issuers were charging “usurious” rates. He contended that the large banks were gouging the middle-class borrower in order to prop up their sagging bottom lines. He also noted that during the mid-1980s credit card issuers had assured Congress that letting the free market work would be the best way to bring credit card rates down, but as of 1991 rates were even higher—this despite a substantial drop in the cost of money.

I would agree with the *Wall Street Journal* and with the economic [sic] professors who say: let the economy work, let the free marketplace work, . . . and you will see interest rates come down . . . . [But] that is not the fact. . . .

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103. Ausubel states this idea in perhaps the most matter-of-fact way possible: “[H]igh interest rates may be essentially neutral from an efficiency point of view. However, they presumably have a strongly undesirable redistributive effect from the comparatively poor (consumers who borrow on credit cards) to the comparatively rich (owners of bank stock).” Ausubel, *supra* note 17, at 75. For views on the conduct of credit card issuers, see *infra* note 110.

104. I do not assert that there are at present no value-based limits on market activity, but the circumstances under which those limits are reached tend to be rather extreme, such as the buying and selling of human beings. American democratic and economic liberalism increasingly seems to require a large measure of ethical neutrality. In 1976, George Wallace argued that “the model of the unregulated market seems to hold an almost magic fascination; unfortunately, the magic tends to bewitch rather than clarify. Although economic analysis helps identify a reform program’s cost and benefits, it also tends to obscure the relevant ethical questions.” Wallace, *supra* note 54, at 497.



... And sure, this may be a popular measure [the interest rate cap amendment], but you know that does not mean it is any less right to say that we should not permit usury, because that is exactly what this is. This is usury.<sup>105</sup>

In his statements about the state of the credit card market, Senator D'Amato had tapped into strong feelings that have long anchored the idea of usury laws. He also pinpointed the tendency of Congress to rely on the "free-market argument" to a fault. But almost more interesting than the comments of Senator D'Amato is the violent reaction they produced. George Will, a highly respected member of the Washington press corps, attacked the Senator in a column that can only be described as vicious.<sup>106</sup> Will stated that D'Amato "could not be trusted to run a lemonade stand, but says he knows just what bank profits are 'fair' and 'comfortable,' what rates are 'reasonable,' 'adequate,' and 'appropriate,' and he knows banks are 'gouging' and 'ripping off' credit card customers in ways that are 'shocking' and 'usurious.'"<sup>107</sup> Will went on to say that D'Amato was "raving" and that it took Senator Jake Garn to inject "fact" into the discussion. Garn had noted that high credit card rates subsidize the less creditworthy and are justified because credit cards do not have secured backing, have high default rates, and are costly to administer.<sup>108</sup>

Senator Garn's comments are easily recognizable as the cost argument, which, as has been demonstrated above, becomes specious when placed in the context of credit card issuers' profits. Yet, in George Will's opinion, Senator Garn spoke the truth, while Senator D'Amato was raving.<sup>109</sup> Regardless of one's opinion of Senator D'Amato or Mr. Will, does the issue of excessive profit-taking not deserve to be discussed? Does one have to hold some special qualifications to question the business practices of an industry? Our broader cultural experience in the form of historical, religious, and ethical learning tells us that societies have long been occupied with these questions. Our nation's most

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105. CONG. REC. S16815-18 (daily ed. Nov. 15, 1991) (statement of Sen. D'Amato concerning his amendment to the Comprehensive Deposit Insurance Reform and Taxpayer Protection Act of 1991, Pub. L. No. 102-242, 105 Stat. 2236 (codified as amended in scattered sections of 12 U.S.C.)).

106. George Will, *Language as Noise: Senate's Credit Card Debacle*, ATLANTA J. & CONST., Nov. 20, 1991, at A11.

107. *Id.*

108. *Id.*

109. *Id.*

important deliberative body seems to be an appropriate place to discuss them.<sup>110</sup>

## 2. Taking Advantage of Weakness

Credit card issuers are well known for bombarding consumers with direct mail solicitations offering credit cards. Certainly, it is up to the individual who receives the solicitation to accept or reject the offer, but in American society as it exists today the temptations that would lead one to accept a card and run up a balance immediately are quite intense. Americans are constantly presented with offers to buy things—in the mail, on the telephone, in the street, on the television, on the radio. There is almost no sanctuary from incessant solicitations. Shopping is even regarded by a substantial portion of the American population as entertainment.<sup>111</sup> We buy things constantly, replacing the not-yet-old with the soon-to-be-obsolete. Compared to Western Europeans, Americans spend more than three times as many hours shopping.<sup>112</sup> Our lives revolve around working and consuming, and some have argued that many Americans are

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110. In an editorial published shortly after the Senate approved a rate cap in 1991, the *New York Times* dismissed the action as “populist folly.” *The Senate’s Credit Card Blunder*, *supra* note 50. On the other hand, letters to the editor of the *Washington Post* following the failure of the credit card interest rate cap legislation give some indication that Senator D’Amato, far from raving, was expressing sentiments that many people shared. Some of the letters read as follows:

The banks say that consumers will be denied credit if a cap is placed on their rates. Well, okay. But who said that was a bad idea? Considering the amount of debt the average family has been forced into to maintain its standard of living, maybe it’s a good idea to let the family pay some of its bills instead of encouraging it to go into debt.

*Letters to the Editor: Give Credit Where Credit is Due*, WASH. POST, Nov. 26, 1991, at A20 (letter from Craig J. Gavin).

Yes, money is getting cheap for the big spenders, but the only access average Americans have to credit is through their cards. Sure, the banks want the rate to remain high, because it is the one area of banking that is operating on a high profit margin. Once again, profit margins are reached on the backs of the middle class and the poor. It is obscene for the same financiers that brought us the S&L crisis and bank failures galore to have access to cheap money while the card-carrying public pays through the nose.

*Id.* (letter from Daniel J. Donoghue).

I strongly suspect that the banks, far from using profits from credit cards to balance unpaid credit cards, are using the profits to balance their own poorly performing loans.

*Id.* (letter from Nancy M. MacKenzie).

111. SCHOR, *supra* note 2, at 107.

112. *Id.*

locked in a vicious cycle of wanting more and more but never being truly satisfied.<sup>113</sup> Because they allow people to shop without money and they make impulse buying easy and convenient, credit cards have fueled this process. In constant dollars, however, real income has declined over the last twenty-five years, and ever-escalating material desires have outpaced people's abilities to satisfy them.<sup>114</sup> Consequently, consumer debt has expanded dramatically.<sup>115</sup>

In a country where economic activity is linked to the powerful cultural themes of individualism and freedom of choice, it is hard to argue that consumers are coerced into buying. Typically, consumers' credit problems are attributed to their own weakness, their lack of self-discipline, or their inability to manage their finances. When pressed by Congress or consumer advocates, credit card issuers suggest that better education on how to use credit will prevent problems related to its abuse.<sup>116</sup> But when a television channel that offers twenty-four-hour shopping is broadcast to millions of people, most of whom have credit cards;

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113. Schor calls this consumerism and materialism "capitalism's squirrel cage." *Id.* at 117-22. Pope John Paul II has made similar observations about life in highly developed capitalist societies. Individuals buy and sell with the goal of replacing something they already have with something better, and they quickly find that the more they have, the more they want, but their deeper needs and aspirations remain unsatisfied. See Pope John Paul II, *Sollicitudo Rei Socialis* [On Social Concern], Encyclical Letter, Dec. 30, 1987.

114. Since 1970, weekly earnings have declined in every private employment sector except services, where wages have remained constant, despite the 1980s boom in the service economy. See, e.g., STATISTICAL ABSTRACT, *supra* note 3, at 457. Credit cards are no doubt helping many Americans maintain lifestyles they cannot afford.

115. Credit card debt more than tripled from 1980 to 1991. *Credit Card Study*, *supra* note 11, at 656. More and more people find it difficult to maintain a "middle class lifestyle" on what they earn, which may explain the dramatic rise in debt among American consumers; some argue that this trend bodes ill for the nation's stability and preservation of its democratic institutions. See Jack Beatty, *Who Speaks for the Middle Class?*, ATLANTIC MONTHLY, May, 1994, at 65-78.

116. See, e.g., *Kiddie Credit Cards: Hearings Before the Subcomm. on Consumer Credit and Insurance of the House Comm. on Banking, Finance and Urban Affairs*, 103d Cong., 2d Sess. 6 (1994) (statement of Gary J. Flood, Senior Vice President, Consumer Cards, MasterCard International) [hereinafter *Hearings*]. Noam Chomsky argues that this "education" is part of an information deluge designed to turn citizens into obedient "atoms of consumption," not savvy consumers. Noam Chomsky, Remarks at Loyola University's Conference on Manufacturing a New World Order: Containing the Crisis at Home and Abroad, Chicago (Oct. 18, 1994) (transcript on file with the *University of Colorado Law Review*). Consumers are supposed to remain "educated," despite being deluged with products and advertisements. On the alienation and cynicism that relentless consumerism has produced in American society, see generally CHRISTOPHER LASCH, *THE TRUE AND ONLY HEAVEN* (1991).

when college students who have never been responsible for their own finances are simply given credit cards; and when credit cards flood the homes of people in all kinds of economic distress, there seems to be a concerted effort to encourage irresponsible financial behavior.<sup>117</sup>

Credit cards make impulse buying easy and financially painless. The desire, or need, to make a particular purchase can be satisfied immediately, while payment can be postponed indefinitely. Most people have no difficulty rationalizing away any concerns about not being able to pay for a purchase at the time of sale by simply assuring themselves that they will have the money when the credit card bill comes due. Others simply accept the fact that they will pay for their purchase over time, regardless of the long-term cost. In either case, there is no need to be concerned about having money to make a purchase.

The way credit cards are marketed to college and university students provides an interesting example of how credit card issuers profit from these predictable behavior patterns. In March of 1994, hearings were held on Capitol Hill by Congressman Joseph Kennedy to examine whether students needed to be protected from aggressive marketing practices by credit card companies.<sup>118</sup> Ruth Susswein, Executive Director of Bankcard Holders of America, a national, nonprofit consumer group, testified that sixty-one percent of the nation's college students have at least one credit card and that cards are being marketed to high school seniors before they even get to college.<sup>119</sup> Many students depend on the cards to pay their expenses, while others simply use them as spending money. Invariably, some of these students encounter serious financial difficulty. Lured by the low minimum payments, they quickly run up huge debts and only realize the seriousness of the problem when they can no longer

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117. Home shopping through television programs has become a growing industry throughout the country and many consumers find themselves charging large sums of money on credit cards to purchase goods advertised on "home-shopping programs." Paul D. Colford, *Shopping At Home With TV As Your Guide*, NEWSDAY, Mar. 2, 1987, Part II, at 4. Consumer groups have warned that television retailers sometimes distort the quality of goods and use tactics that are designed to encourage impulse buying. David Rohde, *If You Shop on Television, Use Caution, Experts Advise*, CHRISTIAN SCI. MONITOR, Aug. 23, 1994, at 8.

118. *Hearings*, *supra* note 116.

119. *Id.* at 4 (statement of Ruth Susswein, Executive Director, Bankcard Holders of America).

pay even the minimums. Most card issuers require no income, credit history, or cosigner before issuing cards to students, but when credit trouble arises, many parents pay the bills, lest their children be saddled with default judgments that would ruin their ability to obtain credit in the future.<sup>120</sup>

Large numbers of young people simply do not understand the concept of debt. Susswein cited a study by the Consumer Federation of America and American Express, which found that seventy percent of the college juniors and seniors interviewed did not know how one maintains or loses a grace period on a credit card and seventy-eight percent did not know the importance of the annual percentage rate (APR) as an indicator of the cost of a loan.<sup>121</sup>

Card issuers responded that students need credit cards and that the vast majority of them use credit cards responsibly. They noted that college campuses are "active marketplaces" and that students have consumer demands similar to other segments of the population. Furthermore, college students, as adults, "have every right to have access to this payment option."<sup>122</sup> Credit cards help initiate young adults into the practices of financial responsi-

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120. *Id.* at 79.

121. *Id.* Such ignorance has led to financial disaster for some of the students appearing before the committee. Although by no means representative of most students, their stories offer insight into the practices of some credit card issuers. The mother of one such student submitted the following to the Subcommittee:

I am here today with my daughter Michele, because she is currently being sued by Signet Bank for \$1,481.55, plus 23.8% interest and threats of attorneys fees for \$370.39. I have tried, since 1992 to get Signet to stop this credit card interest accrual, and settle for 50% of the amount owed. I told the official who is in charge of marketing these cards to students . . . that his bank if [sic] half wrong for marketing these cards to unwary students, and my daughter is half wrong for not understanding what she was getting into when she signed a contract for a long term, high interest loan. They sent me the two page micro type contract, and said she knew what she was signing. . . .

I believe that it is unconscionable for these bank cards to take advantage of a college student's youth, and inexperience. They are ignoring their own sound banking practices by changing the rules to benefit themselves. . . . Banks can not state in their contract that falsely representing one's credit worthiness is a crime, and then turn around and give credit to one who is not credit worthy when it suits their own financial benefit. . . .

*Id.* at 79 (statement of Connie Bedell).

Connie Bedell also noted that she was told by a representative of Discover that the card companies are willing to take risks on college students without incomes because many parents, although they are not responsible for the debt, will pay off a child's card to protect the child's credit rating. *Id.*

122. *Id.* at 54-55 (printed testimony of Visa U.S.A., Inc.).

bility. To assist in that process, MasterCard, Visa, and American Express have developed programs and seminars to educate students on the importance of maintaining a strong credit history and the responsible use of credit.<sup>123</sup>

It makes good business sense to give credit cards to students. Indeed, they are subjected to the same—if not greater—societal pressures to consume as is the rest of the population. More to the point, since most have fairly limited incomes, if they have any income at all, they are probably more likely to carry balances and pay interest. Being a “responsible” credit card customer simply means paying the minimum payment on time every month, which keeps the account current. Most students can do this and most will not want to damage their credit rating by defaulting, but that will not necessarily prevent them from spending irresponsibly.<sup>124</sup> Targeting college students is an effective way to assure that credit card use will become a part of the students’ everyday lives once they enter the workforce.<sup>125</sup> Consumer groups, parents, and members of Congress are reacting against this marketing strategy because it seems inherently manipulative. Youthful indiscretions can mean years of high-interest debt, or worse. Credit card issuers, however, have free rein to use whatever marketing practices they wish. College students represent just one aspect of the overall problem. As credit cards become universally accepted, the pressure increases for all consumers to have one, as does the willingness to take one at whatever terms are offered. The growing use of credit cards to purchase groceries

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123. See, e.g., *id.* at 6-7 (statement of Gary Flood, Senior Vice President, MasterCard International, Inc.).

124. Students represent a huge market for all kinds of products, and there is little in the public discourse encouraging them to delay material gratification. In a culture that increasingly eschews restraint and self-denial, young people are thrust into the marketplace—unsupervised, naive, and with access to easy money. “The consumer society tolerates no deferred gratification between the gleam in the eye and the goods in the hand. It teaches terrible habits—to put off payment but never the acquisition.” Marilyn Gardner, *The Young and the Indebted*, CHRISTIAN SCI. MONITOR, Mar. 31, 1994, at 13.

125. Card issuers want to start an early relationship with their consumers, and studies show that three out of four college students will keep their first credit card for ten to fifteen years. *Hearings, supra* note 116, at 54 (statement of Paul Allen). Some may be using that entire time to pay for a college spending spree. At an interest rate of 16.5%, and assuming no new charges, it would take eight years and eight months to pay off a \$1000 debt with a 2.5% minimum payment per month. The interest payments would total \$766. Ed Avis, *Buried in Debt; Credit Card Offers Aren’t Always a Special Delivery*, CHI. TRIB., July 11, 1994, § 6, at 1.

presents particularly troubling questions. There will no doubt be large numbers of people who will go into debt at high rates of interest in order to keep food on the table.

*C. Rejecting the Free-Market Argument as an Adequate Justification for the Present Interest Rate Policy*

The empirical evidence makes it quite clear that profits in the credit card industry over the last ten years or more have been extraordinary compared to all other types of lending activity. At the same time, the credit card industry has come under attack because the way that industry's money is made—with high interest rates and by handing out credit cards to most anyone—seems driven by greed and has been harmful to many people. Yet, despite widespread disapproval of those practices, the credit card industry has avoided effective interest rate regulation due to a general acceptance of the free-market argument against governmental intervention in these credit transactions. The free-market argument has drawn additional strength from the strong currents of respect for individual autonomy and freedom of choice that run through American culture.

I have shown that by completely rejecting interest rate controls we have embraced and promoted those cultural traits—such as acquisitiveness and competitiveness—that encourage liberal spending, consumption, and the satisfaction of immediate individual desires. At the same time, we have ignored or deemphasized other cultural traits—such as charity towards those in positions of weakness, and disdain for greed and the concentration of wealth—that temper market activity and promote important cultural needs and communal values. Ideally, interest rate controls can be used to create a balance between these seemingly contradictory traits. The current credit card market is not balanced in this respect. Rather, in James Boyd White's terms, the market and its values have been allowed to set behavior standards for the society.<sup>126</sup> Credit cards have moved from being a "luxury" or a "convenience" in a society of savers to a "right" or a "necessity" in a society of spenders. One would be justified in asking whether this change in attitude has really

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126. White, *supra* note 78, at 172-75.

helped consumers, as is often argued by the opponents of interest rate controls, or if it was simply skillful marketing by the credit card industry designed to increase profits.<sup>127</sup>

Determining which cultural values should be promoted by the law in our liberal democratic state has become increasingly difficult.<sup>128</sup> As George Will asked during the 1991 debates on interest rate caps, by what authority can anyone in government determine that certain business practices are "greedy" or "usurious?"<sup>129</sup> In other words, how do we determine what greedy or usurious means? Our society and our legal system have more than enough historical and cultural information to give most Americans a reasonable idea of the meaning of those terms.<sup>130</sup> Meanwhile, credit card issuers continue to make handsome profits. It is clear that the card issuers benefit disproportionately from the current state of the law, but since promotion of the market has become central to our public discussion of this issue, as well as many others, any attempt to "interfere" with the market's "natural" workings is seen as unacceptable.<sup>131</sup>

The premises underlying the free-market argument against interest rate controls are not neutral. A laissez-faire approach benefits aggressive issuers of credit cards who can flood the

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127. I have yet to see an answer to the question, "why *must* people have credit cards?" But for the fact that they have become ubiquitous in this country, there is no evidence that suggests a modern society needs this much unsecured credit to function. Promotion of consumerism has been a successful profit-making tool of American business interests since at least the 1920s, and Americans have been dissatisfied with their material comforts ever since. SCHOR, *supra* note 2, at 118-20.

128. On the effect this phenomenon is having on our ability to govern ourselves, see JAMES D. HUNTER, *BEFORE THE SHOOTING BEGINS: SEARCHING FOR DEMOCRACY IN AMERICA'S CULTURE WAR* (1994).

129. Will, *supra* note 106.

130. As noted above, condemnation of avarice, acquisitiveness, and manipulation of the weak by the strong has found support in Greco-Roman and Judeo-Christian thought, as expressed in the works of Aristotle, the Bible, and various Christian thinkers throughout European history. As part of the Western legal tradition, American law has long drawn on these sources for inspiration, and it is appropriate for it to continue to do so. See *supra* part III.A.

131. Despite the fact that throughout human history unregulated markets have been quite exceptional, discussions of market regulation tend to proceed from the assumption, championed by free-market economists, that the unregulated market is the "natural" state of things. Edward L. Rubin, *Deregulation, Reregulation, and the Myth of the Market*, 45 WASH. & LEE L. REV. 1249, 1264-67 (1988). This is, however, a choice of one among many ways to view the world. "Very often, because the free-market efficiency perspective is an appealing approach and is embedded in our cultural traditions, it will prevail. But it is simply a myth to transform these social choices into transcendent necessities." *Id.* at 1264.



market with their product. It also encourages debt, which card issuers depend upon to realize their profits. The importance of an unregulated interest market to credit card issuers is amply demonstrated by the tremendous lobbying power they have used to defeat interest rate caps. Yet, because the language of the free-market argument is generally accepted as value-free, the unregulated market prevails, whereas attempts to control interest rates are viewed suspiciously as value-laden or "emotional."

#### IV. A PROPOSAL FOR REFORM IN THE CREDIT CARD MARKET

Human life is marked by fits of rational and irrational behavior. Our capacity for completely contradictory acts has shaped human history. From that history we have learned that the law can be used to encourage behavior both noble and vile. Cultures have developed and interpreted these historical experiences and have attempted to promote actions that tend to bring a sense of order to life's chaos. Thus, the law can work in tandem with our larger cultural traditions and encourage that which is best in us, or it can be geared to the needs of the few and justified by appealing to our most selfish instincts.

Credit cards are an important and useful payment device, and although most people who have them appreciate the convenience, no one has a "right" to a credit card. There is always a great deal of temptation to use them in an irresponsible way. Many people find themselves in debt because they cannot resist temptation or perhaps because they are simply irresponsible. Others, however, are driven to use credit cards for all kinds of good reasons—for health care, emergencies, and basic necessities. Credit cards provide quick access to money whenever people think they need it, and people think they need money for both rational and irrational reasons. The law need not tell people when, how, and if they should incur debt, but it can control some of the consequences of indebtedness. At the very least, when interest rate controls are in place, the law does not countenance the taking of outrageous advantage, which comports with a cultural tradition stressing compassion for people in positions of weakness and rejecting the accumulation of wealth for wealth's sake. The credit card industry, however, is engaged only in the business of making money, and it thrives by taking advantage of weakness. This is not to say that the industry should not be free

to pursue profits. Individual consumers must have some measure of accountability for their actions if freedom is to have any real meaning in a democratic society. But it is equally appropriate for the state to control the profit-making impulse.

What typically has been proposed to control interest rates in the credit card market is a floating cap on interest tied to one or more of the major money-market indices, such as the prime lending rate or the yield on Treasury securities. This has an attractive administrative simplicity because credit card issuers are already using these benchmark interest rates for many of their cards. Consumers are also increasingly familiar with floating rates through such vehicles as adjustable-rate mortgages. Furthermore, a floating cap on interest incorporates the economic reality of the ever-changing cost of money in the general economy. The most difficult part of the plan, however, would be setting the "spread" between the benchmark rate and the maximum credit card rate. Using the 1987 and 1991 congressional proposals for federally mandated caps on credit card interest rates produces some interesting results.

The 1987 proposal<sup>132</sup> would have capped credit card rates at eight points above the rate for one-year Treasury securities.<sup>133</sup> Currently, the rate for these securities is approximately 6%, hence the current maximum allowable rate for credit cards under this proposal would be 14%. This is almost four percentage points lower than the average rate charged in 1994. The 1991 proposal<sup>134</sup> would have capped credit card rates at four percentage points over the interest rate charged by the Internal Revenue Service for overdue tax payments.<sup>135</sup> That rate is now 10% and thus would also produce a rate of 14%. Both proposals produce the same rate in 1995, a rate significantly higher than the cost of funds for bank borrowing, the yields on most treasury securities, and the prime lending rate.<sup>136</sup>

Despite the difficulty in finding the most appropriate interest rate spread, a floating cap on interest rates is probably the best

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132. For a discussion of the 1987 proposal, see *supra* part I.B.1

133. See *supra* note 36.

134. For a discussion of the 1991 proposal, see *supra* part I.B.1.

135. Cranford, *supra* note 38.

136. In May of 1995, the federal funds rate was 6%, and the prime lending rate was 9%. *Money Rates*, WALL ST. J., May 9, 1995, at C21. The highest yield on Treasury issues was 7.22% for a 30-year Treasury bond. *Key Interest Rates*, WALL ST. J., May 9, 1995, at C17.

way to set a maximum rate. The easiest benchmark rate to use would be the prime lending rate, because this rate tends to set the standard for a great deal of consumer borrowing. After an initial credit application, many banks offer their customers unsecured lines of credit through checking accounts at two to three percentage points above the prime lending rate. Not everyone who would qualify for a high interest rate credit card would qualify for a line of credit, but by doubling the interest rate spread for credit card interest rates, to six points over prime, credit cards should remain a viable profit-making device for card issuers and available to a large number of consumers. Currently, a six percentage point spread over the prime lending rate would produce a credit card interest rate cap of 15%, which falls in the same range as the 1987 and 1991 proposals.

A top rate of 15% is, of course, much lower than the current average rate.<sup>137</sup> Card issuers would undoubtedly argue that many people will no longer qualify for credit cards. One might question, however, whether it is good business to take credit cards away from people who are currently paying off balances at high interest rates simply because the rate must be lowered. It would be better to have a customer paying a lower interest rate as opposed to having no customer at all.<sup>138</sup> To minimize disruption in the current market, the cap could be phased in over time and credit extended before the cap could be paid off under the original terms.<sup>139</sup>

Interest rate controls in the credit card market would have two major, immediate benefits. First, they would establish some

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137. See *supra* note 21 and accompanying text.

138. Under the current law, with no interest rate restrictions, the number of people who are delinquent is tiny compared to the number of people who keep their accounts current. Typically, 97% of the people who have credit cards have proven they are good credit risks, so it is good business to lend them money. See STATISTICAL ABSTRACT, *supra* note 3, at 522. It would be foolish to drop a steadily paying customer because you cannot charge a higher interest rate. Some profit is better than none at all. Thus, as long as a card issuer can make a profit, common sense would indicate that the number of people who would lose access to credit cards should not be large.

139. As a result of the legal and economic policies of the past few decades, I accept a certain amount of consumer dependence on credit cards as a fact. Given the threats the industry made in 1991, see *supra* note 40, and the realities of interest group politics, consumers would probably be hurt the most in the short term if card issuers revoked a large number of credit cards. A rate cap phased in over time would allow consumers and card issuers to adapt to the changes in a more organized and thoughtful way.

card issuer discipline in a market that distributes credit like so much free candy. Credit card issuers would be forced to screen marginal customers more carefully and would probably be less willing to raise credit limits. More card issuers might be encouraged to use traditional lending standards when issuing credit. Perhaps more issuers would require cosigners or security payments on cards for college students and people with poor credit ratings. Consumers might have less access to credit, but that is not necessarily a negative development. Less unsecured consumer credit in the economy may have socially beneficial effects, such as promoting savings, lowering indebtedness, discouraging impulse buying, and encouraging more community-based and mutual-aid type lending.<sup>140</sup> In sum, the negative side effects of interest rate controls from the perspective of liberal economic theory can be seen as benefits when viewed from a larger cultural and social perspective.

Imposing interest rate controls situates consumer-credit law within the context of a balanced set of societal values. The present market approach projects the message that having the broadest possible market for credit cards is more important than the terms on which that credit is provided. It suggests that the law's primary purpose is to encourage spending and profit-making on whatever terms the market determines are valid. It also promotes a view of individual consumers and suppliers of credit as autonomous actors in the credit market, without any connection to larger community values and standards governing the terms of their bargains or the value to society of their activities.<sup>141</sup> Currently, those who do not strike the best possible deals and those who pay too much or overextend themselves are

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140. For an argument on the macroeconomic benefits of usury laws, see generally Morris, *supra* note 61. In a recent article criticizing the Community Reinvestment Act, which is designed primarily to encourage banks to extend credit to distressed urban communities, Professors Macey and Miller suggest that residents of these areas could meet some of their credit needs by organizing private lending clubs, which are common in many Asian-American communities, rather than relying on commercial lending institutions. Jonathan R. Macey & Geoffrey P. Miller, *The Community Reinvestment Act: An Economic Analysis*, 79 VA. L. REV. 291, 344-46 (1993). Perhaps such self-reliance should be encouraged throughout the society.

141. The Fair Credit and Charge Card Disclosure Act of 1988, *supra* note 36, does mandate that credit card companies provide information on interest rates, payment terms, etc., but increasing the amount of information available in an era of information overload may simply cause consumers to despair of ever obtaining enough information to make truly educated decisions.

considered poor market actors, irrational, or just plain dumb—they deserve what they get.<sup>142</sup> Those who navigate the system successfully have a “right” to whatever benefits come their way. Historically, however, the message of the law and the larger culture has not been so harsh. Both have recognized that although no one wants to be overtaken by debt, for a variety of reasons, people do things that are against their best interests. The law can at least attempt to prevent exploitation.<sup>143</sup>

The most significant challenge to the idea of interest rate controls would be that it is inappropriate for the law to take a moralistic posture that restricts the freedom of individuals to make their own economic bargains and that limits freedom in order for the state to promote certain moral or cultural ideas about how people ought to behave. This challenge assumes, however, that by taking a laissez-faire approach to interest rate regulation, the state is remaining neutral on the question of

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142. In preparing this article, I was struck by how dismissive many people were about the problems individuals might have because of credit cards. There seemed to be an assumption among many that anyone who paid high credit card interest rates was foolish or irresponsible, that they did not “shop around for the best deal,” or that they did not know how to manage their money. Some thought the poor or lower income might deserve protection, but “other people should know better.” There is little compassion for people who show weakness in the marketplace, as if one’s ability in that arena is indicative of one’s worth as a person. No wonder people lie about carrying balances on their credit cards! Rather than wonder what it is about our communal life that causes so many people to carry thousands of dollars of debt on high-interest credit cards, we look at the problem as a sign of individual weakness. This lends credence to White’s theory that the more economic language is used as a justification for various public-policy choices, the more likely it will be that the public will adopt the “selfish” value system in which economic theory is grounded. See White, *supra* note 78, at 197. People also begin to believe that their “rights” are violated when, in order to prevent abuse, the law lays down standards that might cause them some inconvenience.

143. Thomas Jefferson was a passionate advocate of economic independence, which he believed was essential to a strong republic. He was opposed to the concentration of wealth in the hands of the few, and he spoke out against the exploitation of European peasants by the aristocracy. ADRIENNE KOCH, *THE PHILOSOPHY OF THOMAS JEFFERSON* 170-77 (1943). He was sharply critical of the principles of political economy expounded by Adam Smith and preferred the work of the French writer of the same era, Antoine Destutt de Tracy. *Id.* at 181. Tracy saw an inevitable inequality among men caused by ownership of property, which creates two opposing classes—the hired and the hirers. *Id.* at 183. Although he saw this opposition of interests as necessary, he did not see it as an excuse for the blind acceptance of all inequalities as inevitable. “The conclusion which I should draw from it . . . is, that the laws should always endeavor to protect weakness; while too frequently they incline to favour power.” *Id.* (quoting ANTOINE DESTUTT DE TRACY, *A TREATISE ON POLITICAL ECONOMY* (1817)).

consumer and card-issuer behavior. I have shown in this article that "neutrality" in this instance promotes specific business interests and encourages self-centered, acquisitive, market-oriented values. These values are promoted at the expense of other long-standing cultural ideals that have always been a part of Western legal thought and that still find support in society at large, but they are difficult to express in the public sphere because they spring from moral and religious sources. Because our morality is increasingly personalized and Americans have become unwilling to "impose" their values on their fellow citizens, we have little convincing public language that can be used to challenge the purportedly neutral, individually oriented ideals of the marketplace. But all lawmaking involves the promotion of certain values over others. The issue is not so much a choice between legal neutrality on the one hand and the promotion of values on the other. Instead, it is a choice of which values the law will promote.<sup>144</sup> In choosing not to regulate interest rates in the credit card market, we have given free rein to behavioral traits that our society has attempted historically to control. This control has always meant the loss of some individual autonomy and freedom, but history has taught us that the loss was preferable to the alternatives.

## CONCLUSION

The law must encourage standards of behavior for the marketplace that promote human dignity and discourage the abuse of weaker members of society. The current laissez-faire regime has encouraged credit card issuers to pursue unlimited profits without providing boundaries to that pursuit,<sup>145</sup> and it has fueled an irrational consumerism among many credit card holders. It has also contributed to a cheapening of public

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144. The traditional liberal position that the state should remain neutral regarding moral ideas is increasingly under attack, not only by critics of liberalism, but also by supporters of liberalism who believe that a liberal state must be able to promote some moral values. See J. BUDZISZEWSKI, *TRUE TOLERANCE: LIBERALISM AND THE NECESSITY OF JUDGMENT* (1992); Stephen A. Gardbaum, *Why the Liberal State Can Promote Moral Ideals After All*, 104 HARV. L. REV. 1350 (1991).

145. See ARISTOTLE, *supra* note 80. "[A] moral condemnation of great wealth must inform any defense of the free market, and that moral condemnation must be backed up with effective political action." CHRISTOPHER LASCH, *THE REVOLT OF THE ELITES AND THE BETRAYAL OF DEMOCRACY* 22 (1995).

discussions about how we should organize our common life and has diverted attention away from the important issue of American consumers' growing dependence on credit to maintain their lifestyles. Realistic interest rate controls send the important message to both card issuers and consumers that there are limits to what one can do to satisfy desires for money and material goods, as opposed to encouraging a competitive and acquisitive market mentality that tends to benefit the economically powerful. Any inconvenience a limited number of individuals might suffer because they stand to have fewer credit options or lower profits is minimal when compared with the larger societal benefits that would result from using the law to promote community goals beyond the purely economic.